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Supreme Court of the United States

OCTOBER TERM 1947

No. 190-...193

IN PROCEEDINGS FOR THE REORGANIZATION OF A RAILROAD.

IN THE MATTER

of

THE CHICAGO, ROCK ISLAND AND PACIFIC RAILWAY COMPANY,

Debtor.

GERALD AXELROD, *et al.*, constituting the CONVERTIBLE BONDHOLDERS
GROUP, owners of 4½% Gold Bonds of the above-named
Debtor dated May 1, 1930,

Petitioners,

v.

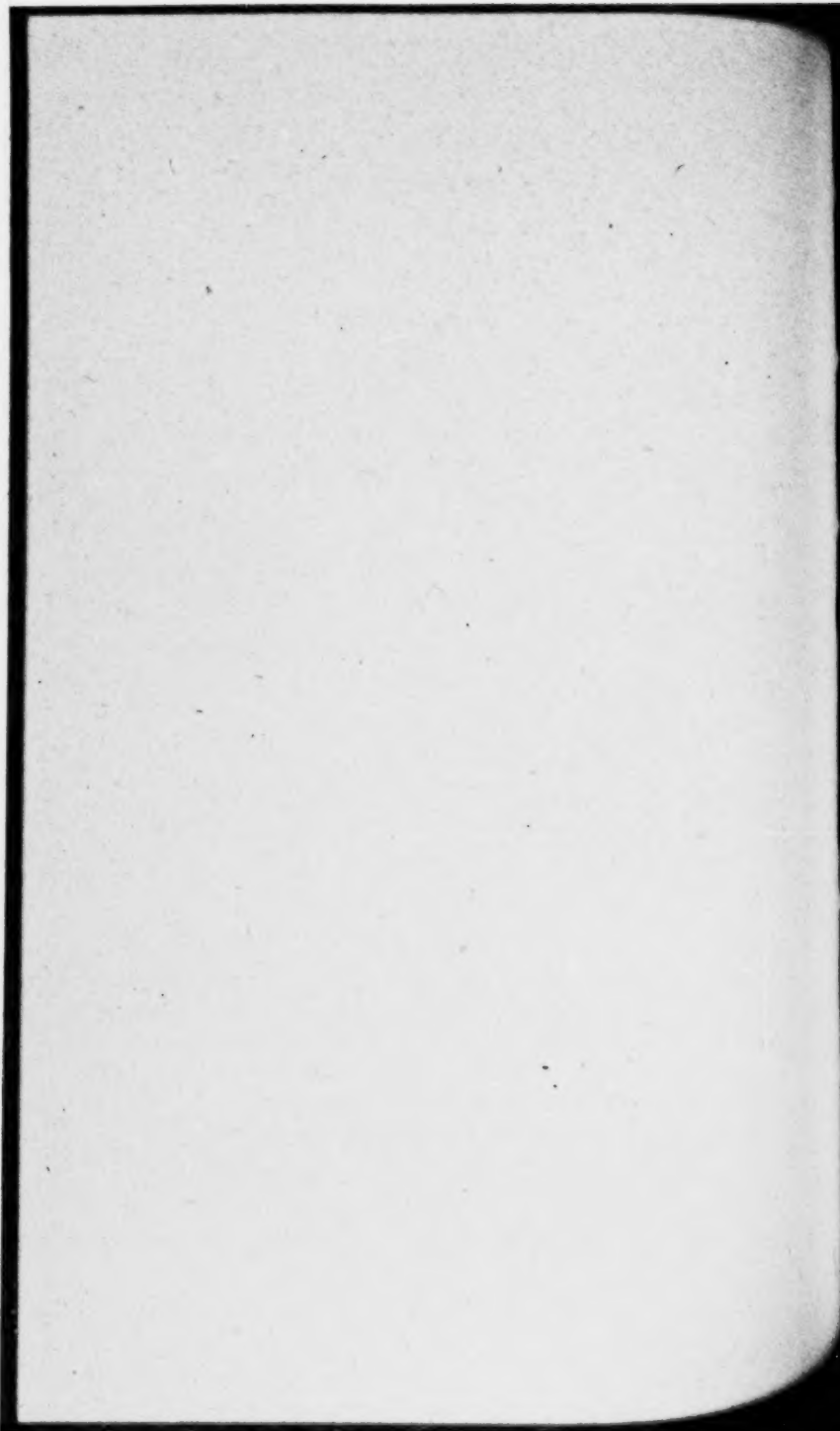
JOSEPH B. FLEMING and AARON COLNOR, as Trustees of THE
CHICAGO, ROCK ISLAND AND PACIFIC RAILWAY COMPANY,
et al.,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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INDEX

	PAGE
Petition for Writ of Certiorari:	
Opinions Below	3
Jurisdiction	3
Statute Involved	5
Statement of Matter Involved	6
Questions Presented	11
Reasons Relied on for Allowance of the Writ	13
Conclusion	17
Appendix "A"	18
Appendix "B"	18
 Brief in Support of Petition:	
Opinions Below	29
Jurisdiction	30
Statement of Case	30
Specification of Errors	30
Summary of Argument (Points I to IX)	33
Conclusion	63
 Appendix:	
Opinion of District Court with Respect to Confirmation of Plan of Reorganization	64
Order of District Court Confirming Plan of Reorganization	73
Order of Circuit Court of Appeals Granting Writ of Mandamus Against District Court Judge Igoe	79

CITATIONS:

	PAGE
Barker v. First Nat'l Bank of Birmingham, 20 Fed. S. 185	37
Bitker v. Hotel Duluth Co., 83 F. (2d) 721, cert. denied 299 U. S. 577	60
Blumgart v. St. Louis, San Francisco R'y Co., 94 F. (2d) 712	59
Bostian v. Levich, 134 Fed. (2d) 284	42
Buffum v. Barceloux Co., 289 U. S. 227	34
Central Railroad of N. J., In re: 136 Fed (2d) 633, cert. denied 320 U. S. 805	38
Chase Nat'l Bank v. Chicago, R. I. & P. R'y Co., 294 U. S. 648	2, 33, 36, 61
Chicago, Rock Island & P. R'y Co., In Re:	
157 F. (2d) 241	38
160 F. (2d) 942, 949	30
162 I. C. C. 611	4, 14
175 I. C. C. 46	4, 14
249 I. C. C. 297	51
242 I. C. C. 298	6, 7, 53, 56, 61
247 I. C. C. 533	6
257 I. C. C. 307	6, 7, 39
257 I. C. C. 265	6, 7, 32, 49, 51
252 I. C. C. 483	39
Continental Ill. Nat'l Bank v. Chicago, Rock Island & P. R'y Co., 294 U. S. 648	39
Ecker v. Western Pacific R'y Co., 318 U. S. 448	50
Fierman v. Seward Nat'l Bank of N. Y., 61 Fed. (2d) 952, cert. den. 288 U. S. 613	38
Fleming v. Traphagen, 155 Fed. (2) 889 reversed in 67 Sup. Ct. 365	3
Fleming et al. v. Traphagen, 329 U. S. 686	3, 61
Gardner v. State of New Jersey, 329 U. S. 565	40
Gilmore v. U. S., 93 Fed. (2d) 774, cert. den. 304 U. S. 569	55
Hultzman v. Tevis, 82 Fed. (2d) 940	42
In re Central R. Co. of N. J., 136 Fed (2d) 633, 1320 U. S. 805	38
In re Chicago, Rock Island & P. R'y Co.	
157 F. (2d) 241	38
160 F. (2d) 942, 949	30
162 I. C. C. 611	4, 14

INDEX

iii

	PAGE
175 I. C. C. 46	4, 14
242 I. C. C. 298	6, 7, 53, 56, 61
247 I. C. C. 533	6
252 I. C. C. 483	39
257 I. C. C. 307	6, 7, 39
257 I. C. C. 265	6, 7, 32, 49, 51
249 I. C. C. 297	51
In re Roth Company, 125 Fed. (2d) 396	41
In re Times Square Auto Supply Co., 47 Fed. (2d) 240, cert. den. 283 U. S. 856	38
Institutional Investors v. Chicago, Milwaukee, St. P. & P. R. Co., 318 U. S. 523	42
Irving Trust v. Deutsch, 73 Fed. (2d) 121	37
Jackson v. Smith, 254 U. S. 586	34, 37
Lilienthal v. U. S., 97 U. S. 237	55
Magruder v. Drury, 235 U. S. 106	34
Meinhard v. Salmon, 249 N. Y. 458, 164 N. E. 545	34, 37
Munson v. Syracuse, 103 N. Y. 58	37
N. Y. Life Ins. Co. v. Stoner, 109 F. (2d) 874	55
Phyle v. Phyle, 199 N. Y. 538	37
Reconstruction Finance Corp'n v. Denver, Rio Grande W. R. R. Co., 66 Sup. Ct. 1282	42, 43
Reliance Life Ins. Co. v. Burgess, 112 F. (2d) 234, cert. den. 304 U. S. 569	55
U. S. v. Dunn, 268 U. S. 121	34
Williamson v. Williams, 137 Fed. (2d) 298	42

STATUTES AND AUTHORITIES.

PAGE

Bankruptcy Act as amended:

Section 24 (c)	4, App. "B"
Section 60	4, 5, 33, App. "B"
Section 77 (Section 205 U. S. C. A.)	4, 5, 11, 12, 13, 38, 41, 43, 61, App. "B"
Section 77 (b)	19, 54, App. "B"
Section 77 (d)	22, 49, App. "B"
Section 77 (e)	4, 5, 12, 15, 16, 24, 32, 40, 42, 43, 49, 54, 62, App. "B"
Section 77 (p)	2

Federal Rules of Civil Procedure, Rule 52 (a)	41
---	----

Fifth Amendment to the Constitution of the United States	3, 5, 18, 38
--	--------------

Judicial Code Section 240 (a)	4
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THE CHICAGO, ROCK ISLAND AND PACIFIC RAILWAY COMPANY,
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holders Group, owners of the 4½% Gold Bonds of the
Debtor, dated May 1, 1930,

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v.

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The Chicago, Rock Island and Pacific Railway Com-
pany, et al.,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

TO: THE HONORABLE CHIEF JUSTICE AND THE ASSOCIATE
JUSTICES OF THE SUPREME COURT OF THE UNITED
STATES:

Petitioners, individual bondholders of the \$32,228,000.00
issue of the 4½% Convertible Gold Bonds of the above

named debtor dated May 1, 1930, to become due May 1, 1960, constituting the Convertible Bondholders Group pursuant to Section 77 (p) of the Bankruptcy Act as amended, and the orders of the Interstate Commerce Commission (hereinafter referred to as "I. C. C." or "Commission") and the District Court of the United States for the Northern District of Illinois, Eastern Division (hereinafter referred to as "District Court") authorizing the same, and being sole spokesmen in this proceeding for said bond issue, respectfully pray that a writ of certiorari issue to review the order and decree of the United States Circuit Court of Appeals for the Seventh Circuit, rendered on February 21st, 1947, which reversed the order and decree of the United States District Court for the Northern District of Illinois, Eastern Division, entered June 28th, 1946, which District Court order denied confirmation to a plan of reorganization and remanded the plan to the Commission for reconsideration and revision; and to review the subsequent Circuit Court order dated June 9th, 1947 (see appendix to brief page 77 herein) issued in pursuance thereto commanding the District Court to enter an order of confirmation forthwith in form satisfactory only to the proponents of the plan.

In this petition, Petitioners rely upon the transcript of Record filed by Appellants in the Circuit Court below on September 23rd, 1946, and November 1st, 1946 (Transcript of Record Nos. 9203-9208) (page reference to which is hereinafter referred to as "R"). The Additional Transcript of Record, filed by Petitioners, is referred to as "Add. R". Printed portions of transcript of record, designated Appendix "A" in said Court is hereinafter referred to as "TR".

This petition is related to the appeal, decided by this Court in *Chase National Bank, et al. v. Chicago, Rock Island & Pacific Ry. Co.*, 294 U. S. 648, wherein certain

bank creditors were restrained from foreclosing the debtor's collateral security for their loans.

This petition is further related to the appeal, in this proceeding, decided by this Court in the October, 1946 term (No. 454) wherein it was held that holders of Choctaw & Memphis bonds were not entitled to interest upon accumulated interest representing part of their claim against this debtor: *Fleming et al. v. Traphagen*, 155 Fed. (2d) 889, certiorari granted and order reversed, 329 U. S. 686.

Opinions Below

The opinion of the District Court denying confirmation of the plan and remanding it back to the Commission was filed on June 28th, 1946. Said opinion has not been reported but a true copy thereof is in the record (R. 249-255).

The opinion of the Circuit Court of Appeals reversing the District Court was entered on February 21st, 1947. Said opinion has not been reported as yet, but a true copy thereof is in the Additional Transcript of Record (Add. R. 332-343).

The opinion of the Circuit Court relating to the Choctaw & Memphis bonds is reported in 155 Fed. (2nd) 889. The order of the Circuit Court was reversed by this Court by *per curiam* opinion in *Fleming et al. v. Traphagen*, 329 U. S. 686.

Jurisdiction

Jurisdiction of this Court is invoked under the "due process" clause of the Fifth Amendment to the Constitution of the United States; under the provisions of

Section 77, Section 60 and Section 24 (c) of the Bankruptcy Act; under Section 240 (a) of the Judicial Code.

Jurisdiction of this Court is invoked by reason of the reversal by the Circuit Court of Appeals, Seventh Circuit, of the order of the District Court, and the requirement by the Circuit Court of Appeals that the District Court find, as a matter of law, that the plan is fair and equitable and must be confirmed. On June 6, 1947, the said Circuit Court granted a writ of mandamus summarily commanding the District Court Judge to confirm the plan forthwith. (See *infra*, p. 77.)

Jurisdiction is invoked, further, to determine whether the Circuit Court of Appeals may under Section 77 properly review the decision of the District Court remanding the plan to the I. C. C. prior to the action of the I. C. C. pursuant thereto, to determine whether such a review by the said Circuit Court is not in fact a denial of "due process".

Jurisdiction is invoked, further, because the following questions of public policy of transcendent importance are involved:

(A) Whether railroad bonds, such as the \$32,228,000 Convertible Bonds of the debtor, duly authenticated by a Federal agency (the I. C. C.) in May, 1930, and approved again in 1931 as secured over 300% in capital value (175 I. C. C. 46; 162 I. C. C. 611—Finance Docket 8177), and as so authenticated sold to the public, can be practically eliminated as of no substantial value by the same Federal agency upon a plan in reorganization commenced 23 months thereafter;

(B) Whether the "cram-down" provisions of Section 77 (e) of the Bankruptcy Act should be enforced against the will of such bondholders compelling their acceptance of such a plan where more than 76% of them have voted pursuant to law to reject the plan and where the District

Court has found as a fact that said creditors were justified in rejecting the plan as not fair and equitable to them.

(C) Whether such a plan, formulated and based upon pre-war earnings, should be enforced against non-consenting security holders where changes in circumstances since the last consideration of the plan by the I. C. C. and changes since the approval of the plan by the District Court (*i. e.* unanticipated large current post-war earnings, debt reduction and increased liquid assets) have rendered the plan obsolete and inequitable.

Jurisdiction is invoked, further, to determine finally whether, upon confirmation proceedings after rejection of the plan by one or more classes of creditors, the burden of establishing fairness of the plan under the Statute, is upon the proponents or whether the burden of establishing unfairness is upon the dissenting creditors.

A motion for rehearing, reconsideration and modification, and for stay of mandate was duly entered in said Circuit Court of Appeals on March 11th, 1947, which motion was denied by said Court on April 7th, 1947. On May 20, 1947 said Circuit Court denied a further application for an order recalling its mandate and for a stay of proceedings pending application to this honorable Court for a writ of certiorari.

Statute Involved

The "due process" clause of the Fifth Amendment to the Constitution of the United States and the pertinent provisions of Sections 77 and 60 of the Bankruptcy Act, particularly Subsection (e) thereof, are directly involved in this appeal. These provisions may be found herein (pp. 18-27).

Statement of Matter Involved

Petitioners respectfully seek a review of the order of the United States Circuit Court of Appeals, Seventh Circuit, and a stay of enforcement of the orders based upon its decision of February 21st, 1947, which reversed the order of the District Court, instructed the District Court to confirm the plan forthwith and then commanded the District Judge to enter the order of confirmation in the form submitted by the proponents of the plan.

Unsatisfied creditor claims of over \$80,000,000 are involved in this proceeding (257 I. C. C. 265; TR. 234).

The amount of Convertible Bondholders' claims, including both principal and interest, is \$47,697,440. It is the fourth largest creditor class. The principal amount is \$32,228,000. Under the plan \$31,290,335 of said claims are eliminated.

The plan of reorganization was adopted by the I. C. C. in October, 1940 (242 I. C. C. 298; TR. 31). The capitalization of the reorganized debtor was then determined at \$351,180,912 (242 I. C. C. 298, pp. 478-489; TR. 142); increased in July, 1941, by the I. C. C. to \$368,127,410 (247 I. C. C. 533, pp. 578-579; TR. 168); and again decreased in May, 1944, to \$356,117,327 (257 I. C. C. 307, p. 325; TR. 249).

The net railway operating income, before annual fixed interest charges from the time the plan was formulated to 1946, inclusive, as reported to the I. C. C., was as follows:

1938	\$ 2,512,843
1939	5,458,853
1940	8,133,477
1941	17,616,382
1942	36,557,111
1943	36,794,983
1944	26,079,690
1945	22,195,944
1946	17,248,000

Said income for the first three months of 1947 exceeded that of the first three months of 1946 by over \$1,100,000, or over 25%. At the present rate of traffic Rock Island should earn \$25,000,000 this year, or twice the present interest charges.

The annual fixed interest charges under the proposed recapitalization were set by the I. C. C. at not more than \$2,400,000 (TR. 142). The I. C. C. was of the opinion in October, 1940 (242 I. C. C. 298; TR. 142), that "earnings available for interest and dividends of approximately \$11,000,000 in a prospective normal year are reasonably well supported by the evidence of record." The Commission in said report rejected a forecast of net operating income of \$12,500,000 for the year 1944 as "somewhat too high" (TR. 142). The Commission has held no hearings nor has it received any further evidence in this proceeding since September, 1943 (257 I. C. C. 265, 266; TR. 227), and held hearings at that time only with respect to certain specific matters entirely unrelated to the treatment of junior creditors under the plan (257 I. C. C. 265, 266; TR. 227) which matters were referred to it by order of the District Court (TR. 297).

Besides over \$80,000,000 in unsatisfied secured claims and general claims, more than \$129,000,000 in equity claims (Common and Preferred Stock) are eliminated by the plan (257 I. C. C. 307, Appendix; TR. 259).

The I. C. C. thereafter entered an order directing the various classes of creditors to vote approval or disapproval of the plan. On February 26th, 1946, the I. C. C. announced the results of the balloting. Two classes of creditors, the Convertible Bondholders represented by your petitioners herein and the Little Rock and Hot Springs Bondholders lien creditors, rejected the plan by a 75.78% and a 80.62% majority, respectively.

On March 13th, 1946, the proceeding came before the District Court on a hearing to confirm the plan. The Court adjourned the hearing, and stated:

"You have the picture of a company with approximately Seventy-eight Million Dollars in cash* or funds available to be readily converted into cash in its treasury.

You have a first mortgage bond issue of approximately Sixty Million Dollars and unpaid interest on that bond issue of Twenty-one or Twenty-two Million Dollars.

There is enough cash in this treasury to pay off one of these first mortgages which totals the sum of Sixty Million Dollars and upon which there is approximately Twenty-one or Twenty-two Million Dollars of unpaid interest.

What the man on the street cannot understand is why that mortgage cannot be paid off, and something left for the junior security holders and something left for the stockholders.

From all I see of this picture; from all I hear about it and about what is said in connection with this lawsuit, I am more and more coming to a point where I think the entire matter, perhaps, should be sent back to the Interstate Commerce Commission for a re-examination of this entire situation, and, in that way, let everybody know exactly what is involved and how these different interests are going to be cared for; and at the same time, these bondholders can have their day in court and these stockholders can have their day in court" (R. 138-140).

On June 28th, 1946, the adjourned date, after hearing was held and testimony was received, the District Court

* Now over \$83,000,000.

rendered its decision and opinion, including findings of fact and conclusions of law, denying confirmation of the plan, and remanding the plan to the I. C. C. for rehearing and reconsideration (R. 249-254).

By order dated July 18th, 1946, the I. C. C. reopened the proceedings and assigned the same for public hearing. Several consecutive petitions for postponement were filed by the Respondents and granted by the Commission. Thereafter, the I. C. C., upon Respondents' further petition for postponement, cancelled its order and directed that no hearings be held for re-examination of the plan.

On February 21st, 1947, the Circuit Court of Appeals reversed the order of the District Court and directed the District Court to find, in effect, that the plan was fair and equitable to all classes of creditors and to confirm the plan.

On the hearing before the District Court in the proceedings for confirmation the proponents of the plan offered no testimony in support of their position, and introduced only one exhibit, a statement showing the comparison between the estimated income account figures for the first five months of 1946 and the actual figures for the same period of the prior year (R. 239-240). A drop in operating income for the year was indicated by that estimate.

All of the testimony at the hearing, and all exhibits other than the one above mentioned were introduced by the opponents of the plan. The combined effect of the oral testimony and the exhibits offered by the proponents of the plan show the following (R. 242-248):

A.) The wartime earnings of the railroad were far in excess of the earnings of any pre-war year. This fact is shown not only as a guide to present and expected post-war earnings, but to demonstrate the substantial improvement in the financial structure of the debtor since the last consideration by the I. C. C. The facts found by the Dis-

trict Court, quoted below, are a direct result of the income earned by the road during and following the war period.

B.) The immediate post-war earnings were somewhat less than the top wartime earnings, but greatly in excess of the "\$11,000,000 prospective normal year." Attempt has been made by the proponents of the plan to make capital of this drop in earnings. It is respectfully submitted that if, on the one hand, wartime earnings are not to be taken as a guide to prospective earnings, it is similarly improper to consider the drop from wartime earnings to immediate post-war earnings as evidence of a continuing downward trend in the road's earnings. As a matter of record, current earnings are at more than twice the "\$11,000,000 prospective normal year," and are continuing to rise.

C.) The post-war earnings are substantially higher than the earnings for the periods considered by the I. C. C. in its initiation of the plan. The upward trend of post-war earnings is shown by later figures, not a part of the record before the District Court but part of the official I. C. C. records, to be continuing, indicating a far more optimistic prognosis than the I. C. C. could possibly reach from the figures available to it in the pre-war period in which the plan was conceived.

As a result of the testimony adduced by the opponents of the plan, the District Court found the following, as shown by its opinion:

"In the present case we have a plan that, except for slight modifications, was prepared by the Commission in 1940 and rests on studies of earnings, etc., going back to 1937 and even beyond.

Against that we find the Debtor today with cash, or equivalent of over \$70,000,000*; with an R. F. C. loan aggregating, principal and interest, in excess of \$18,000,000, paid in full; with over 20% of the Choctaw

* Now over \$83,000,000.

& Memphis first mortgage retired; and with an amazing reduction, in the interim, of equipment debt. Three classes of creditors set up in the original plan have disappeared—the banks, the R. F. C., and the Peoria Railway Terminal Co.

The above recital does not take into account the tremendous sums expended over the period on improvement of road and equipment, nor does it include the retirement of debt on jointly-owned facilities such as the Joliet and Denver terminals" (R. 252).

Questions Presented

Although more than \$80,000,000 in creditor claims and \$129,000,000 in equity claims are eliminated under this pre-war plan, this honorable Court has never heard argument on it. It is the only instance of a Class I railroad undergoing reorganization under Section 77 of the Bankruptcy Act whose plan has not been so considered by this Court.

The review requested herein raises questions of the greatest public and legal importance.

Has the discretion of the District Court in refusing confirmation of the plan and remanding it for reconsideration after a proper hearing of the merits been so abused as to require reversal by the Circuit Court of Appeals?

Is not the shortcut method advocated by the Circuit Court of Appeals of compelling confirmation of the plan, a taking of petitioners' property without due process of law?

Is the Circuit Court of Appeals justified in considering the fairness of the plan after the plan has been duly remanded to the I. C. C. by the District Court before the I. C. C. has acted upon such remanding order, in the absence of a gross abuse of discretion by the District Court?

Has the Circuit Court of Appeals the right to require the District Court to find that the plan is fair and

equitable and that the non-consenting creditors were not justified in rejecting the plan after the District Court has found to the contrary after a hearing pursuant to the provisions of Section 77 (e) of the Bankruptcy Act.

Is the Circuit Court justified in commanding the District Court Judge by mandamus to enter an order of confirmation forthwith under, under such circumstances in form satisfactory only to the proponents of the plan?

The above questions have never been decided by this Court since this proceeding is the first proceeding under Section 77 of the Bankruptcy Act wherein the District Court has refused confirmation and the Circuit Court of Appeals has reversed the order of the District Court and ordered confirmation.

When an approved plan of reorganization is rejected by one or more classes of creditors, and a hearing in confirmation proceedings is held before the District Court pursuant to Section 77 (e) of the Bankruptcy Act, is the burden of establishing fairness of the plan to the dissenting creditors upon the proponents of the plan or is the burden of establishing unfairness upon the non-consenting creditors?

In the absence of any testimony establishing fairness of the plan to dissenting classes of creditors or lack of justification for the rejection of the plan by non-consenting creditors, may the appellate court nevertheless find that the plan is fair and equitable and that the rejection was unjustified and thereby order confirmation of the plan?

Should a plan of reorganization proceed to confirmation where the courts have made substantial modifications to the plan without the prior action and approval of the I. C. C.?

Is the present plan fair and equitable to all classes of creditors?

Should the present plan of reorganization, formulated and based upon a pre-war level of earnings, be applied to the debtor when its post war earnings and financial status are now far greater than pre-war, and are continuing to improve substantially? This question has never been passed upon by this Court.

Should a plan be confirmed when it is tainted with the fact that the trustee for the Convertible Bondholders, still nominally, actively appearing in their behalf, has had individual, conflicting dealings with the debtor to its own benefit and to the detriment of the Convertible Bondholders?

Should such a plan be confirmed when, although rejected by the Convertible Bondholders, the said plan gives the indenture trustee the power of nomination of a reorganization manager for said Bondholders?

Should the present plan be confirmed in the face of a declaration by one of the trustees of the debtor that, by means of reasonable refinancing, certain claims, wiped out by the present plan, could be paid in full? (See Statement of Aaron Colnon, Trustee, submitted simultaneously herewith.)

Reasons Relied On for the Allowance of the Writ

This Honorable Court should allow the writ since unsettled constitutional and bankruptcy questions of the greatest public importance are involved.

This Court has never before considered or passed upon an appeal in a reorganization case under Section 77 of the Bankruptcy Act wherein the District Court has denied confirmation to a plan remanding the plan to the I. C. C. for reconsideration, and the Circuit Court of Appeals has, without allowing the I. C. C. to reconsider the plan, reversed the order of the District Court and instructed the District Court to confirm the plan.

The law is not settled as to the authority or jurisdiction of the Circuit Court to compel the District Court to confirm a plan of reorganization which the District Court has found to have been formulated during the depression years, and to have been based upon pre-war, depression years' level of earnings, and which the District Court has found to be obsolete and unfair and inequitable to the dissenting classes of creditors.

This 1938 plan eliminates over \$80,000,000 in creditor claims and more than \$129,000,000 in preferred and common stock equities. Hence the question here arises of judicial approval being given to a fraud perpetrated against the convertible bondholders and the public generally since this reorganization proceeding was commenced only 23 months after the I. C. C. approved the sale to the public of this \$32,228,000 issue of bonds (175 I. C. C. 46; 162 I. C. C. 611).

Neither the District Court nor the Circuit Court allowed the Petitioners to be heard concerning the pledge of the debtor's collateral to the Chase National Bank, then Trustee for the Convertible Bondholders, in its individual capacity; the foreclosure of such collateral; and the issue of new securities under the plan on the basis of the ownership of such collateral instead of on the basis of the original indebtedness. Since the collateral represents 262% of the value of the original claim, the Petitioners, junior creditors, are deprived of their property without due process of law.

The question of the burden of proof in confirmation proceedings, not heretofore passed upon by this Court, should be settled by a definitive statement of this Court.

Confirmation of the plan after it has been modified by the Court without the prior consent of the I. C. C. constitutes the deprivation of the Petitioners' property without due process of law.

The law is not settled as to whether the Circuit Court has the right to compel the District Court "to be satisfied and find" that the plan is fair and equitable to dissenting creditors and thereby apply to such creditors the "cram down" provisions of Section 77(e) of the Bankruptcy Act.

The reorganization managers required to be appointed under the plan are senior creditor designees. The Convertible Bondholders, junior creditors should have the right to selection of at least one manager of their own choosing.

This honorable Court should also determine:

A.) Whether the dual and conflicting role played by the Chase National Bank in this proceeding was not inimical to the interests of its *cestuis que* trust, the Convertible Bondholders.

B.) Whether the collateral belonging to the Debtor and foreclosed by the Chase National Bank is not still in the custody of the court.

C.) Whether the present plan of reorganization does not discriminate unfairly in favor of the senior creditors.

D.) Whether the present plan of reorganization is now fair and equitable when, since its adoption, the debtor after having distributed \$50,420,522 to its creditors, has additional increased assets of \$185,241,485 including \$83,000,000 in cash and the annual fixed charges proposed by the plan have been reduced through payment of debt from earnings by \$625,973 and when, nevertheless, the plan proposes to give all new senior securities and 90% voting control of the new company to the present senior creditors.

E.) Whether the Petitioners were deprived of a full hearing on material objections to the plan by the limitations and restrictions contained in the order of the District Court referring the plan to the I. C. C. for modification, dated June 25th, 1943.

F.) Whether post war earnings should not now be taken into consideration by the courts and by the I. C. C. in arriving at a fair valuation of the debtor's assets.

G.) Whether the I. C. C. should not now be given an opportunity to consider the advisability of the payment of the general mortgage and thus procure additional assets available for distribution to junior creditors.

H.) Whether the Choctaw & Memphis Bondholders and the general mortgage bondholders are not being overcompensated under the plan.

I.) Whether a plan now shown to be unfair should be confirmed.

J.) Whether, in the absence of any evidence offered on the hearing in the confirmation proceedings to show that the plan is fair and equitable, confirmation should not be denied as a matter of law.

K.) Whether the Respondents have met the burden of proof necessary under Section 77(e) of the Bankruptcy Act to permit confirmation of the plan after it has been rejected by two classes of creditors.

L.) Whether among other changes in the plan, the effective date thereof should not be brought up to date from the present effective date of January 1, 1944 in order to prevent the granting of interest on interest, a practice condemned by this Court in Fleming, et al. v. Traphagen, page 3, supra?

M.) Whether the exercise of the "cram-down" provision of § 77(e) against petitioners and the short-cut procedure advocated by the Circuit Court of Appeals is not a taking away of petitioners' property without due process of law.

Conclusion

Petitioners respectfully submit that the decision and orders of the Circuit Court of Appeals were erroneous and without authority in law, that the questions here involved are constitutional questions and are of general public importance, and that it is in the public interest to have those questions answered as soon as practicable by an authoritative decision of this Court.

WHEREFORE, the Petitioners respectfully pray that a writ of certiorari be issued out of and under the seal of this honorable Court, directed to the United States Circuit Court of Appeals for the Seventh Circuit, directing immediate reinstatement of the decree and order of the District Court or in the alternative directing that Court to certify and send to this Court for its review and determination on a day certain to be named therein, a transcript of the record and proceedings herein and that the decree of said Court be reviewed, to the end that the judgment herein of said Circuit Court of Appeals be reversed and the decree and order of the District Court for the Northern District of Illinois, Eastern Division be reinstated; and that the Petitioners may have such other and further relief in the premises as to this Court may seem just and proper.

Dated: New York, N. Y., July 4, 1947.

HARRY KIRSHBAUM,
MICHAEL GESAS,
Counsel for Petitioners.

Appendix "A"

FIFTH AMENDMENT

TO THE

CONSTITUTION OF THE UNITED STATES.

No person shall be held to answer for a capital, or otherwise infamous crime unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation. (Emphasis ours.)

Appendix "B"

The Bankruptcy Act, as amended:

Sec. 24(c). The Supreme Court of the United States is hereby vested with jurisdiction to review judgments, decrees, and orders of the Circuit Court of Appeals of the United States and the United States Circuit Court of Appeals for the District of Columbia in proceedings under this title in accordance with the provisions of the laws of the United States now in force or such as may hereafter be enacted. (11 U. S. C. A. section 47(c).)

* * * *

Sec. 60. Preferred creditors

(a) A preference is a transfer, as defined in this title, of any of the property of a debtor to or for the benefit of a creditor for or on account of an antecedent debt, made or

Appendix "B"

suffered by such debtor while insolvent and within four months before the filing by or against him of the petition in bankruptcy, or of the original petition under chapters 10, 11, 12 or 13 of this title, the effect of which transfer will be to enable such creditor to obtain a greater percentage of his debt than some other creditor of the same class. For the purposes of subdivisions a and b of this section, a transfer shall be deemed to have been made at the time when it became so far perfected that no bona-fide purchaser from the debtor and no creditor could thereafter have acquired any rights in the property so transferred superior to the rights of the transferee therein, and, if such transfer is not so perfected prior to the filing of the petition in bankruptcy or of the original petition under chapter 10, 11, 12 or 13 of this title, it shall be deemed to have been made immediately before bankruptcy. (11 U. S. C. A. Sec. 96.)

(b) Any such preference may be avoided by the trustee if the creditor receiving it or to be benefited thereby or his agent acting with reference thereto has, at the time when the transfer is made, reasonable cause to believe that the debtor is insolvent. Where the preference is voidable, the trustee may recover the property or, if it has been converted, its value from any person who has received or converted such property, except a bona-fide purchaser from or lienor of the debtor's transferee for a present fair equivalent value: *Provided, However, That* where such purchaser or lienor has given less than such value, he shall, nevertheless, have a lien upon such property, but only to the extent of the consideration actually given by him. Where a preference by way of lien or security title is voidable, the court may, on due notice, order such lien or title to be preserved for the benefit of the estate, in which event such lien or title shall pass to the trustee. For the purpose of any recovery or avoidance under this section, where plenary proceedings

Appendix "B"

are necessary, any State court which would have had jurisdiction if bankruptcy had not intervened and any court of bankruptcy shall have concurrent jurisdiction. (Tit. 11, U.S.C.A., Sec. 96-b.)

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Sec. 77(b) A plan of reorganization within the meaning of this section (1) shall include provisions modifying or altering the rights of creditors generally, or of any class of them, secured or unsecured, either through the issuance of new securities of any character or otherwise; (2) may include provisions modifying or altering the rights of stockholders generally, or of any class of them, either through the issuance of new securities of any character, or otherwise; (3) may include, for the purpose of preserving such interests of creditors and stockholders as are not otherwise provided for, provisions for the issuance to any such creditor or stockholder of options or warrants to receive, or to subscribe for, securities of the reorganized company in such amounts and upon such terms and conditions as may be set forth in the plan; (4) shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in light of its earnings, experience, and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; (5) shall provide adequate means for the execution of the plan, which may include the transfer of any interest in or control of all or any part of the property of the debtor to another corporation or corporations, the merger or consolidation of the debtor with another corporation or corporations, the retention of all or any part of the property by the debtor, the sale of all or any part of the property of the debtor either subject to or free from any lien at not

Appendix "B"

less than a fair upset price, the distribution of all or any assets, or the proceeds derived from the sale thereof, among those having an interest therein, the satisfaction or modification of any liens, indentures, or other similar interests, the curing or waiver of default, the extension of maturity dates of outstanding securities, the reduction in principal and/or rate of interest and alteration of other terms of such securities, the amendment of the character of the debtor, and/or the issuance of securities of either the debtor or any such other corporation or corporations for cash, or in exchange for existing securities, or in satisfaction of claims or rights or for other appropriate purposes; and may deal with all or any part of the property of the debtor; may reject contracts of the debtor which are executory in whole or in part, including unexpired leases; and may include any other appropriate provisions not inconsistent with this section.

The adoption of an executory contract or unexpired lease by the trustee or trustees of a debtor shall not preclude a rejection of such contract or lease in a plan of reorganization approved hereunder, and any claim resulting from such rejection shall not have priority over any other claims against the debtor because such contract or lease had been previously adopted. The term "securities" shall include evidences of indebtedness either secured or unsecured, bonds, stock, certificates of beneficial interest therein, certificates of beneficial interest in property, options, and warrants to receive, or to subscribe for, securities. The term "stockholders" shall include the holders of voting-trust certificates. The term "creditors" shall include, for all purposes of this section all holders of claims of whatever character against the debtor or its property, whether or not such claims would otherwise constitute provable claims under this Act, including the holder of a claim under a contract executory in whole or in part including an unexpired lease.

Appendix "B"

The term "claims" includes debts, whether liquidated or unliquidated, securities (other than stock and option warrants to subscribe to stock), liens, or other interests of whatever character. For all purposes of this section unsecured claims, which would have been entitled to priority if a receiver in equity of the property of the debtor had been appointed by a Federal court on the day of the approval of the petition, shall be entitled to such priority and the holders of such claims shall be treated as a separate class or classes of creditors. In case an executory contract or unexpired lease of property shall be rejected or shall not have been adopted by a trustee appointed under this section, or shall have been rejected by a receiver in equity in a proceeding pending prior to the institution of a proceeding under this section, or shall be rejected by any plan, any person injured by such nonadoption or rejection shall for all purposes of this section be deemed to be a creditor of a debtor to the extent of the actual damage or injury determined in accordance with principles obtaining in equity proceedings. The provisions of section 96 of this title shall apply to a proceeding under this section. For all purposes of this section any creditor or stockholder may act in person or by an attorney at law or by a duly authorized agent or committee subject to the provisions of subsection (p) of this section. The running of all statutes of limitation shall be suspended during the pendency of a proceeding under this section. (11 U. S. C. A. Section 205(b).)

Sec. 77(d). The debtor, after a petition is filed as provided in subsection (a) of this section, shall file a plan of reorganization within six months of the entry of the order by the judge approving the petition as properly filed, or if heretofore approved, then within six months of August 27, 1935, and not thereafter unless such time is extended by the judge from time to time for cause shown, no single extension at any one time to be for more than six months.

Appendix "B"

Such plan shall also be filed with the Commission at the same time. Such plans may likewise be filed at any time before, or with the consent of the Commission during, the hearings hereinafter provided for, by the trustee or trustees, or by or on behalf of the creditors being not less than 10 per centum in amount of any class of creditors, or by or on behalf of any class of stockholders being not less than 10 per centum in amount of any such class, or with the consent of the Commission by any party in interest. After the filing of such a plan, the Commission, unless such plan shall be considered by it to be prima facie impracticable, shall, after due notice to all stockholders and creditors given in such manner as it shall determine, hold public hearings, at which opportunity shall be given to any interested party to be heard, and following which the Commission shall render a report and order in which it shall approve a plan, which may be different from any which has been proposed, that will in its opinion meet with the requirements of subsections (b) and (e) of this section, and will be comparable with the public interest; or it shall render a report and order in which it shall refuse to approve any plan. In such report the Commission shall state fully the reasons for its conclusions.

The Commission may thereafter, upon petition for good cause shown filed within sixty days of the date of its order, and upon further hearings if the Commission shall deem necessary, in a supplemental report and order modify any plan which it has approved, stating the reasons for such modification. The Commission, if it approves a plan, shall thereupon certify the plan to the court together with a transcript of the proceedings before it and a copy of the report and order approving the plan. No plan shall be approved or confirmed by the judge in any proceeding under this section unless the plan shall first have been

Appendix "B"

approved by the Commission and certified to the court. (11 U. S. C. A. section 205(d).)

Sec. 77(e). Upon the certification of a plan by the Commission to the court, the court shall give due notice to all parties in interest of the time within which such parties may file with the court their objections to such plan, and such parties shall file, within such time as may be fixed in said notice, detailed and specific objections in writing to the plan and their claims for equitable treatment. The judge shall, after notice in such manner as he may determine to the debtor, its trustee or trustees, stockholders, creditors, and the Commission, hear all parties in interest in support of, and in opposition to, such objections to the plan and such claims for equitable treatment. After such hearing, and without any hearing if no objections are filed, the judge shall approve the plan if satisfied that: (1) It complies with the provisions of subsection (b) of this section, is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; (2) the approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of such hearing, are reasonable, are within such maximum limits as are fixed by the Commission, and are within such maximum limits to be subject to the approval of the judge; (3) the plan provides for the payment of all costs of administration and all other allowances made under or to be made by the judge, except that allowances provided for in subsection (c), paragraph (12) of this section, may be paid

Appendix "B"

in securities provided for in the plan if those entitled thereto will accept such payment, and the judge is hereby given power to approve the same.

If the judge shall not approve the plan, he shall file an opinion, stating his conclusions and the reason therefor, and he shall enter an order in which he may either dismiss the proceedings, or in his discretion and on motion of any party in interest refer the proceedings back to the Commission for further action, in which event he shall transmit to the Commission a copy of any evidence received. If the proceedings are referred back to the Commission, it shall proceed to a reconsideration of the proceedings under the provisions of subsection (d) of this section. If the judge shall approve the plan, he shall file an opinion, stating his conclusions and the reasons therefor, and enter an order to that effect, and shall send a certified copy of such opinion and order to the Commission. The plan shall then be submitted by the Commission to the creditors of each class whose claims have been filed and allowed in accordance with the requirements of subsection (c) of this section, and to the stockholders of each class, and/or to the committees or other representatives thereof, for acceptance or rejection, within such time as the Commission shall specify, together with the report or reports of the Commission thereon or such a summarization thereof as the Commission may approve, and the opinion and order of the judge: *Provided*, that submission to any class of stockholders shall not be necessary if the Commission shall have found, and the judge shall have affirmed the finding, (a) that at the time of the finding the corporation is insolvent, or that at the time of the finding the equity of such class stockholders has no value, or that the plan provides for the payment in cash to such class of stockholders of an amount not less than the value of their equity, if any,

Appendix "B"

or (b) that the interests of such class of stockholders will not be adversely and materially affected by the plan, or (c) that the debtor has pursuant to authorized corporate action accepted the plan and its stockholders are bound by such acceptance: *Provided further*, That submission to any class of creditors shall not be necessary if the Commission shall have found; and the judge shall have affirmed the finding, that the interests of such class of creditors will not be adversely and materially affected by the plan, or that at the time of the finding the interests of such class of creditors have no value, or that the plan provides for the payment in cash to such class of creditors of an amount not less than the value of their interests. For the purpose of this section the acceptance or rejection by any creditor or stockholder shall be in writing, executed by him or by his duly authorized attorney, committee, or representative. If the United States of America, or any agency thereof, or any corporation (other than the Reconstruction Finance Corporation) the majority of the stock of which is owned by the United States of America, is a creditor or stockholder, the interests or claims thereof shall be deemed to be affected by the plan, and the President of the United States, or any officer or agency he may designate, is hereby authorized to act in respect of the interests or claims of the United States or of such agency or other corporation. The expense of such submission shall be certified by the Commission and shall be borne by the debtor's estate. The Commission shall certify to the judge the results of such submission.

Upon receipt of such certification, the judge shall confirm the plan if satisfied that it has been accepted by or on behalf of creditors of each class to which submission is required under this subsection holding more than two-thirds in amount of the total of the allowed claims of such

Appendix "B"

class which has been reported in said submission as voting on said plan, and by or on behalf of stockholders of each class to which submission is required under this subsection holding more than two-thirds of the stock of such class which has been reported in said submission as voting on said plan; and that such acceptances have not been made or procured by any means forbidden by law: *Provided*, That, if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provisions for fair and equitable treatment for interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of this subsection (e): *Provided further*, That if, in any reorganization proceeding under this section, the United States is a creditor on claims for taxes or customs duties (whether or not the United States has any other interest in, or claim against, the debtor, as creditor or stockholder), no plan which does not provide for the payment thereof shall be confirmed by the judge except upon the acceptance, certified to the court, of a lesser amount by the President of the United States or the officer or agency designated by him pursuant to the provisions of the preceding paragraph hereof: *Provided, further*, That if the President of the United States or such officer or agency shall fail to accept or reject such lesser amount for more than ninety days after receipt of written notice so to do from the court, accompanied by a certified copy of the plan, the consent of the United States insofar as it claims for taxes or customs duties are concerned shall be conclusively presumed. If the judge shall confirm the

Appendix "B"

plan, he shall enter an order and file an opinion with a statement of his conclusions and his reasons therefor. If the judge shall not confirm the plan, he shall file an opinion, with a statement of his conclusions and his reasons therefor, and enter an order in which he shall either dismiss the proceedings, or, in his discretion and on the motion of any party in interest, refer the case back to the Commission for further proceedings, including the consideration of modifications of the plan or the proposal of new plans. In the event of such a reference back to the Commission, the proceedings with respect to any modified or new plan shall be governed by the provisions of this section in like manner as in an original proceeding hereunder.

If it shall be necessary to determine the value of any property for any purpose under this section, the Commission shall determine such value and certify the same to the court in its report on the plan. The value of any property used in railroad operation shall be determined on a basis which will give due consideration to the earning power of the property, past, present, and prospective, and all other relevant facts. In determining such value only such effect shall be given to the present cost of reproduction new and less depreciation and original cost of the property, and the actual investment therein, as may be required under the law of the land, in light of its earning power and all other relevant facts. (11 U. S. C. A. section 205(e).)

Supreme Court of the United States

OCTOBER TERM 1947

No.

— ♦ —
IN PROCEEDINGS FOR THE REORGANIZATION OF A RAILROAD.

IN THE MATTER

of

THE CHICAGO, ROCK ISLAND AND PACIFIC RAILWAY COMPANY,
Debtor,

GERALD AXELBOD, et al., constituting the Convertible Bond-
holders Group, owners of 4½% Gold Bonds of the
Debtor, dated May 1, 1930,

Petitioners,

v.

JOSEPH B. FLEMING and AARON COLNON, as Trustees of
The Chicago, Rock Island and Pacific Railway Com-
pany, et al.,

Respondents.

— ♦ —
BRIEF IN SUPPORT OF PETITION FOR WRIT OF
CERTIORARI TO THE UNITED STATES CIRCUIT
COURT OF APPEALS FOR THE SEVENTH CIRCUIT

Opinions Below

The opinion of the Circuit Court of Appeals for the
Seventh Circuit was entered on February 21st, 1947, and

is reported in 160 F. (2d) 942 and 949. A true copy is in the Additional Transcript of Record (Add. R. 332-343). The opinion of the District Court was filed on June 28th, 1946, and has not been officially reported. A true copy thereof is in the record (R. 249-255).

The opinion of the District Court and the order of said Court confirming the plan of reorganization is attached hereto as an appendix (*post*, p. 62). There is also attached as part of said appendix, the order of the Circuit Court granting the motion for the issuance of a writ of mandamus commanding the District Judge to confirm the plan of reorganization in the form submitted by respondents (*post*, p. 77).

Jurisdiction

A statement of the constitutional, statutory and other grounds upon which the jurisdiction of this Court is invoked is contained in the Petition (p. 3), and, to avoid duplication, is not repeated here.

Statement of Case

A statement of the case is set forth in the Petition under the heading "Statement of Matter Involved" and, to avoid duplication, is not repeated here.

Specification of Errors

The Circuit Court of Appeals erred:

1. In adopting an unauthorized short-cut procedure of reviewing the decision of the District Court remanding the plan to the I. C. C., prior to reconsideration of the plan by the I. C. C.

2. In ruling that the District Court abused its discretion in refusing confirmation to the plan, despite the fact that the preponderance of credible evidence supported the decision of the District Court.

3. In ruling that the Chase National Bank, in the dual and conflicting role of trustee for the Convertible Bondholders and as holder of collateral for loans privately extended to the Debtor without knowledge or consent of the Convertible Bondholders was not violating its position as fiduciary and not acting prejudicially to the Convertible Bondholders in the treatment accorded to them in the plan of reorganization ordered confirmed by the Court, particularly since the plan, rejected by the Convertible Bondholders, requires the said Chase National Bank to choose a reorganization manager on behalf of Convertible Bondholders.

4. In holding that the plan of reorganization is fair and equitable and compatible with the public interest and that it complies with the provisions of Section 77 (e) of the Bankruptcy Act.

5. In holding that the plan of reorganization affords due recognition to the rights of the Convertible Bondholders and that the same does not discriminate unfairly in favor of the holders of preferred securities.

6. In holding that the General Mortgage bondholders were only fully compensated under the plan, when it is clear that they receive interest on accumulated interest and are otherwise overcompensated.

7. In holding that the R. F. C. collateral returned to the trust estate should remain undistributed, despite the ruling of the I. C. C. that the payment of the R. F. C. claims "would necessitate material modification in the plan"

(257 I. C. C. 265, 272), despite the interim distribution to senior creditors of \$50,000,000 in cash and securities and despite the fact that the Convertible Bondholders are virtually excluded from the plan.

8. In ordering confirmation of an outmoded plan of reorganization for the Debtor, a plan formulated and adopted prior to the commencement of the war (1937-1940) and based upon depressed earnings, etc., of that period.

9. In ordering confirmation of a plan of reorganization which was altered in several material respects by the District Court without resubmission to or re-examination by the I. C. C.

10. In failing to assign to the Proponents of the plan the burden of establishing the fairness of the plan to dissenting classes of creditors and in failing to recognize that such burden has not been met.

11. In ordering confirmation of a plan which eliminates the unsecured creditors claims and also any control or management of the reorganized company by said creditors and by enforcing the "cram-down" provisions of Sec. 77 (e) of the Bankruptcy Act as amended.

12. In denying Petitioners' application for reargument and reconsideration of its opinion and order of February 21st, 1947.

13. Upon the granting of the writ of mandamus against the District Court (pp. 77-80, *post*) and upon such other errors as may appear to this Court, not assigned or specified herein.

Summary of Argument

I

The plan of reorganization, as it now stands, countenances illegal preferential treatment in favor of the Chase Bank Group for first mortgage collateral privately obtained from the Debtor without consent of the Convertible Bondholders by allocating to them 262% of the amount of their claim in new, choice securities at the direct expense of the Convertible Bondholders who remain virtually excluded from participation in the plan of reorganization. The facts concerning said preference loan are set forth in "R. 4-22." This honorable Court without knowledge of the fiduciary relationship of the Chase Bank to the Convertible Bondholders, or the preferential nature of said loans, enjoined the foreclosure and sale of the Debtor's collateral (*Chase Nat'l Bank, et al. v. Chicago, R. I. & P. R'y. Co.*, 294 U. S. 648).

Said plan, which thus rewards such conduct of a trustee by permitting it to retain or foreclose said collateral in lieu of payment as was done with the R.F.C. loans, is a fraud upon the *cestuis que* trust, the Convertible Bondholders, and is unjust, unfair, inequitable and incompatible with the public interest.

Section 60 of the Bankruptcy Act, as amended,
page 18, infra;
Buffum v. Barceloux Co., 289 U. S. 227, 236.

The Chase Bank Group* should be held to account as a trustee *ex malificio* for its conduct to the extent of the value of the collateral which it improperly acquired. In

* The names of the banks constituting the Chase Bank Group are set forth in this Court's opinion in 294 U. S. 648; also see R. 7, par. 16.

its illegal dual capacity, it competes with the Convertible Bondholders and under the plan secures favored treatment contrary to the interests of the Convertible Bondholders.

Buffum v. Barceloux Co., 289 U. S. 227, 236;
U. S. v. Dunn, 268 U. S. 121;
Jackson v. Smith, 254 U. S. 586, 588;
Magruder v. Drury, 235 U. S. 106;
Meinhard v. Salmon, 249 N. Y. 458, 164 N. E. 545, per Cardozo, J.

A plan of reorganization which approves, accepts and recognizes this wrongful discrimination against the Convertible Bondholders should not be confirmed.

The Chase Bank is here in a dual capacity; on its own behalf and as trustee to the Convertible Bondholders. Its duties as Trustee to the Convertible Bondholders is covered by no agreement, but is basic in law and equity. It injected itself later as a privately secured creditor. This it could not legally do.

The erroneous impression has been forced upon the Court that the obligations and duties of the Chase Bank as Trustee for the Convertible bonds is set forth in a trust indenture of some kind to which all the Convertible Bondholders are party. It has been called an "Indenture Trustee" by the Court. Perhaps the Chase Bank entered into an agreement in writing with the debtor—but no Convertible Bondholder was ever a party to any such Indenture or agreement. The Chase Bank nevertheless, received compensation, commissions, fees, etc., as such Trustee.

The duty, loyalty and fidelity of a Trustee towards his beneficiary does not depend on contract or agreement. It is basic in the public policy of the community. The

law is elementary and clear that even where there is the bare possibility of a conflict of interest, the trustee must yield.

The Chase Bank in its dual capacity, with interests conflicting and loyalties divided, committed many serious breaches of trust.

The first breach of trust was the application by the Chase Bank as Trustee of the proceeds of the Convertible bond issue to the payment of its own bank loan made to the debtor. The Chase Bank knew the purposes for which this proposed \$32,228,000 bond issue was sought, for which it was going to act as Trustee. It sought to protect its own loan, rather than that of the Convertible Bondholders' equity.

The second breach of trust was its subsequent retainer from the debtor of \$15,589,000 in face value collateral for its own loan, without first getting the consent of the Convertible Bondholders or even notifying them.

The third and simultaneous breach of trust occurred with the making of the bank loans as short term loans. By extending these loans for only three (3) months the Banks thereby made certain that they could not be repaid, that it would thereupon be enabled to foreclose on its collateral long before the 1960 maturity date of the Convertible bonds, and thus foreclose the Convertible Bondholders.

The fourth breach of trust occurred with the failure of the Chase Bank to turn over this collateral to its bondholders as received from the debtor to better secure the Convertible Bondholders' position and its silence or refusal to reveal its dual interests to this Court or to account to the Convertible Bondholders for its action.

The fifth breach of trust occurred when the Chase Bank and the other Banks demanded and received from

the debtor, 50% payment on account of its own collateral loans on August 1st, 1932, in the sum of \$4,125,000 thus inducing the debtor's insolvency. Payment was demanded and accepted without regard to the impairment of the debtor's equity and of its ability to meet its obligations to the Convertible Bondholders and in destruction of the entire value supporting the Convertible bonds.

The sixth and seventh breaches of trust occurred when the Banks, including the Chase Bank, as Trustee, retaining all the collateral, nevertheless accepted from the debtor said 50% payment of their loans in the sum of \$4,125,000 thus further securing their position and further impairing the equity behind the Convertible bonds.

The eighth breach of trust occurred when the Banks, including the Chase Bank, as Trustee, foreclosed on the collateral and on the equity supporting the Convertible bonds. This was in gross violation of their fiduciary duty and of the letter and spirit of the opinion and order of this Court in *Chase Nat'l Bank, et al. v. Chicago, Rock Island & P. R'y Co.*, 294 U. S. 648.

The inaction, indifference and disregard to the Convertible Bondholders' interests by the Chase Bank as Trustee, and their participation in eliminating their bondholders' equities is a dereliction of its duty unbecoming a loyal Trustee.

The law requires as we have shown, that the Chase Bank as Trustee shall not have conflicting loyalties nor individually act in a manner which may be calculated to or tend to adversely affect the interests and welfare of the *cestui que trust*, the Convertible bondholders.

The ninth breach of trust occurs in the appointive power of reorganization managers, exercised under the plan by the Chase Bank in concert with the proponents of the plan which gives the Chase Bank continued control which should be in the hands of the Convertible Bondholders.

In the proposed plan the Chase Bank has:

- (1) A controlling allocation of new securities for itself against the interest and welfare of its bondholders.
- (2) Competed with its bondholders in thus securing favored treatment for itself in the Plan against the interests and welfare of its bondholders.
- (3) An illegal dual position of conflicting interests which was never disclosed to the Court except by these petitioners. The mere conflicting relationship makes the Bank loans illegal. See *Phyle v. Phyle*, 199 N. Y. 538; *Munson v. Syracuse*, 103 N. Y. 58, 74; *Barker v. First National Bank of Birmingham*, 20 Fed. S. 185; *Meinhard v. Salmon*, 249, N. Y. 458, at page 463.
- (4) By committing several serious breaches of trust thereby jeopardized and destroyed the equity supporting the Convertible bonds.

By acting in concert and participating with them in all matters affecting the making and foreclosure of the loans, with full knowledge of the facts, the other Banks are in *pari delicto* with the Chase Bank. See *Irving Trust v. Deutsch*, 73 Fed. (2d) 121, at pages 124, 125; *Jackson v. Smith*, 254 U. S. 586, 41 Sup. Ct. 200; since in so doing, it deprived the Convertible Bondholders of their equity, bringing nearer the insolvency of the debtor.

The plan recognizes the trust relationship of the Chase Bank to the Convertible Bondholders in appointing the Chase Bank as reorganization manager for them and also approves the illegal conduct of the Chase Bank toward its bondholders.

This situation cannot be permitted in any plan which seeks confirmation by the Court.

II

The denial, by the District Court and the Circuit Court, to the Petitioners of a hearing on objections under Section 77 of the Bankruptcy Act, as amended, relating to the Chase Bank Group's unlawful acquisition of the Debtor's collateral and the preferential treatment afforded to said Group under the plan of reorganization which adversely affected the Convertible Bondholders' interest, was unconstitutional and constituted a deprivation of property without due process of law.

Fifth Amendment to the Constitution of the United States, Appendix A, page 18;

In re Central R. Co. of N. J., 136 Fed. (2nd) 633, cert. den. 320 U. S. 805;

Fierman v. Seward Nat'l. Bank of N. Y., 61 Fed. (2nd) 952, cert. den. 288 U. S. 613;

In re Times Square Auto Supply Co., 47 Fed. (2nd) 240, cert. den. 283 U. S. 856.

In the opinion upon approval of the plan, the Circuit Court said:

"Appellants' counsel, in his brief and again in oral argument, urged that the Chase National Bank as trustee for the issue of unsecured convertible bonds and the holder of collateral for loans extended to the debtor was in the exercise of a dual and conflicting role and that in the exercise of this dual role, the bank violated its position as fiduciary to the convertible bondholders by retaining or conveying to others the property of the debtor. A consideration of the cogency of such argument is not related to the merits of the plan of reorganization which is the question before this court. The contentions of the convertible bondholders must be denied." 157 F. (2d) 241.

Similarly, in proceedings to confirm the plan at each step, these petitioners raised the same argument and each time the lower courts refused to consider this question on the grounds that it was not material to the plan.

The relevancy of petitioners' argument is shown by the following facts:

(a) The transaction whereby the Chase Bank Group secured over \$15,985,000 of collateral for \$3,811,006 in loans was completed within three months prior to the commencement of these reorganization proceedings.

(b) The allocation of new securities under the plan was made to the Chase Bank Group not on the basis of actual claims but on the basis of the liquidation value of the collateral held by these bank creditors (252 I. C. C. 483, 487).

(c) As a result the present plan actually allots to the Chase Bank Group \$15,805,003 or over 262% of their claims in cash and new choice securities (257 I. C. C. 307, App. A, p. 318).

(d) The Chase Bank Group also receives under the plan a controlling allocation of new securities and the power in concert with the proponents of the plan to appoint four out of the five reorganization managers which carries with it the actual right to appoint the first board of directors of the reorganized company (TR. 26-27).

(e) The Convertible Bondholders have no manager representation under the power of appointment set forth in the plan (TR. 26).

The securities involved in this phase of the reorganization are still within the jurisdiction of the court, and equitable distribution of them can still be made.

Continental Illinois National Bank & Trust Co. v. Chicago, Rock Island & Pacific R. Co., 294 U. S. 648.

And in *Gardner v. State of New Jersey*, 329 U. S. 565, decided January 20, 1947, this Court held that the property of the debtor remains in the custody of the Court, irrespective of where the property may be located, and the reorganization court has full jurisdiction over all questions respecting the title to such property.

The action of the Circuit Court is a taking of petitioners' property without due process of law.

III

The disposition of the plan after rejection by one or more classes of security holders rests within the discretion of the District Court, not the Circuit Court of Appeals.

The Bankruptcy Act, Section 77 (e), reads, in part, as follows:

"If the judge shall not confirm the plan, he shall file an opinion, with a statement of his conclusions and his reasons therefor, and enter an order in which he shall either dismiss the proceedings, or, in his discretion and on the motion of any party in interest, refer the case back to the Commission for further proceedings, including the consideration of modifications of the plan or the proposal of new plans. In the event of such a reference back to the Commission, the proceedings with respect to any modified or new plan shall be governed by the provisions of this section in like manner as in an original proceeding hereunder."

The order of the District Court, refusing to confirm the plan, contained the following findings of fact (R. 254):

The order of the District Court, refusing to confirm the plan, contained the following findings of fact (R. 254):

"And the Court being satisfied and finding, in the light of the additional evidence presented at said hear-

ings on June 11, 1946, (a) that the plan does not make adequate provision for fair and equitable treatment for the interests or claims of the holders of the Convertible Bonds, (b) that the rejection of the plan by the holders of the Convertible Bonds was reasonably justified in the light of the respective rights and interests of the holders of the Convertible Bonds and all the relevant facts, (c) that the plan does not conform to the requirements of clause (1) of the first paragraph of subsection (e) of Section 77 of the Bankruptcy Act, as amended, in respect of its treatment of the holders of the Convertible Bonds, * * *".

Presumably there was a dispute about these facts, else the decision of the Circuit Court would not have even an apparent basis. Since there was a controversy about the facts, the decision of the Circuit Court in *In re Roth Company*, 125 Fed. (2nd) 396, applies. In that case the Court said:

"Determination of abuse of discretion involves the exercise, by us, of sound judgment upon the facts. If there is a controversy as to the facts, and if the facts themselves largely define the wisdom of the discretion, review by the appellate court is seldom effective and it should not be. The appellate court's review does not include trial court's discretion."

To the same effect are the Rules of Civil Procedure. Rule 52 (a) provides in part:

"Findings of fact shall not be set aside unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the credibility of witnesses."

It has been repeatedly held by the appellate courts that, where a question of fact is involved, and on the facts decided by the District Court the discretion of that Court was

exercised, such exercise of discretion will not be reversed by the appellate courts unless a gross abuse of discretion is shown.

Bostian v. Levich, 134 Fed. (2nd) 284;
Williamson v. Williams, 137 Fed. (2nd) 298;
Hultzman v. Tevis, 82 Fed. (2nd) 940.

This principle was followed by this Court in *Reconstruction Finance Corp. v. Denver & Rio Grande Western Railroad Company*, 66 Sup. Ct. 1282, wherein this Court said, at page 1302:

“The grounds accepted by us in former sections of this opinion as sustaining, as of January 1, 1943, the valuation of the road, the allocation of the securities, and the treatment of cash, war earnings and capital reductions establish that for the act of confirmation on November 29, 1944, over the objection of the General bondholders, the finding of the judge that the plan then made ‘adequate provision for fair and equitable treatment’ of the dissenters was justified. 62 Fed. Supp. at page 390. *In view of the District judge’s familiarity with the reorganization, this finding has especial weight with us.*” (Italics ours.)

And in the case of *Institutional Investors v. Chicago, Milwaukee, St. P. & P. R. Co.*, 318 U. S. 523, this Court said, at page 564:

“We would have a different problem if the District Court had failed to perform the functions which Section 77 (e) places upon it. But it cannot be said that there is any such failure here. The District Court satisfied itself that the principles of priority as applied to these facts were respected. See 36 Fed. Supp. pp. 202, 203, 211, 212. Since such a determination rests in the realm of judgment rather than mathematics,

there is an area for disagreement. But we are not performing the functions of the District Court under Section 77 (e). Our role on review is a limited one. It is not enough to reverse the District Court that we might have appraised the facts somewhat differently. If there is warrant for the action of the District Court, our task on review is at an end."

The action of the Circuit Court was unauthorized in law and constitutes a taking of petitioners' property without due process of law.

IV

Sufficient, substantial evidence was presented to the District Court to justify the remanding of the plan.

In *Reconstruction Finance Corp. v. Denver & Rio Grande Western R. Co.*, 66 Sup. Ct. 1282, this Court, in discussing the Congressional intent in passing Section 77, said, at pages 1289 and 1290:

"The answer reached by Congress was that the experience and judgment of the Commission must be relied upon for final determination of value and of matters affecting the public interest, subject to judicial review to assure compliance with Constitutional and statutory requirements. This was the interpretation of all members of this court from the language of the act and the evidence of Congressional purpose in the hearings, reports and discussions."

Further, at page 1296:

"Assuming that the courts, as courts with equity powers in a bankruptcy matter, might set aside a plan, fair and equitable when adopted by the Commission, merely on account of subsequent changes in economic conditions of the region or the nation, *it should not be*

done when the changes are of the kind that were envisaged or considered by the Commission in its deliberations upon or explanations of the plan." (Italics added.)

The District Court, in its opinion, stated:

"In the present case we have a plan that except for slight modifications was prepared by the Commission in 1940 and rests on earnings, etc., going back to 1937 and even beyond" (R. 252).

The facts about to be discussed could not possibly have been "envisaged or considered by the Commission in its deliberations" upon the plan, for they came into existence several years later.

With these legal principles in mind, we may consider the evidence supporting the District Court's decision.

Before the District Court upon the hearing to confirm the plan was a breakdown of the net receipts from operations of the entire road for each year from 1936 to and including 1945 (Debtor's Ex. 2, R. 242). It shows that:

For the year 1937, the year mentioned by the District Court as the basic year in the Commission's consideration, the net earnings of the corporation before payment of interest obligations amounting to \$12,890,237 were \$3,333,357. This represents a net loss at stock level of \$9,556,880. For 1945 the net earnings before allowance for interest of \$12,461,380 amounted to \$20,444,571, leaving a net profit at stock level of \$7,983,191. Gross income increased from \$4,984,614 in 1937 to \$23,281,765 in 1945, an increase to well over 400%. Net profits for 1947 are running well ahead of these figures. (See statement of Aaron Colnon, Trustee, submitted simultaneously herewith.)

These figures alone indicate a clear necessity for the I. C. C. to make an up to date correction of the computa-

tions upon which the plan now under consideration was based. A reading of the original I. C. C. report will demonstrate how inaccurate was their forecast of earnings upon which forecast the present plan is based.*

It cannot be denied no matter how considered that four full years of wartime operations have brought into the general fund huge profits which themselves have had a substantial effect on the capital condition of the Debtor. It is this factual change in capital position, and the demonstrated continued earnings of similar magnitude, which constitutes the justification for the remanding of the plan.

However, we do not depend upon wartime earnings to determine that the old valuations are so erroneous from the present point of view as to require remanding of the plan. For the year 1946, the only full, post-war calendar year, the net profits after taxes but before interest amounted to \$17,248,000. The interest requirements under existing capitalization are \$12,285,004. Thus the net profit at stock level amounts to \$4,962,996. This showing was made despite the fact that the period was a period of labor unrest, strikes and general industrial stagnation normal to the early post-war period; despite the fact that a large wage increase was given the railroad employees, retroactively to January 1, 1946, which was charged against the net operating income; and despite the fact that an increase in freight rates, which would have produced at least \$12,000,000 additional profits in 1946, did not take effect until January 1st, 1947 (Report of Chicago, R. I. & P. R. Co. to the stockholders, dated March 21, 1947).

That the earnings trend is upward, not downward, is evidenced by the fact that the reported gross operating income

* For example the Commission said: "the evidence of record convinces us that the estimate by the first and refunding committee of \$12,500,000. of earnings available for interest in a normal year is somewhat too high." TR. 142.

of the road for the first three months of 1947 is more than 25% over that of the same period of 1946, and the net operating income for 1947 will exceed \$25,000,000 (Report of Aaron Colnon, Trustee to United States Senate, on S. 249, dated May 16, 1947, submitted simultaneously herewith).

These figures indicate that under the present capital structure there is still some value left for stock interests after all creditors are fully compensated. Certainly they indicate that the Convertible Bondholders are entitled to far greater, if not full, compensation.

The figures also give rise to some novel questions, questions not yet passed upon by any appellate court. Should not *post-war* earnings be considered by the I. C. C. in its evaluations? Should not the post-war period be considered a normal period of operation? The answer to these questions is not purely legal. There is a factual phase which should be passed upon by the I. C. C. before they are submitted to the courts for judicial determination.

The post-war operating figures of the railroad were never before the I. C. C. We cannot rely upon the "experience and judgment of the Commission" as this Court has urged that we should, if we do not afford the Commission the opportunity to consider the existing conditions. Nor were these later figures before the District Court on the occasion of the approval of the plan. Hence, they constitute reasonable justification for the rejection of the plan by the Convertible Bondholders arising after approval, within the meaning of the decision in the *Denver* case. Certainly they constitute sufficient new evidence to justify the District Court's remanding the plan.

In addition to the vastly increased earnings, other relevant facts were brought to the attention of the District Court which justify the remanding of the plan.

Mentioned in the opinion of the District Court is the fact that the R.F.C. loans, aggregating over \$18,000,000, were paid in full. There should be considered, also, the concomitant fact that such payment released to the general fund collateral valued at over \$40,000,000. Whether or not the actual payment of the loan affects the capital structure of the Debtor, there is a substantial effect created by the return of the collateral, measured by the difference between the value of the collateral and the amount paid. The difference is approximately \$22,000,000.

The reduction of debt in the hands of the public should also be considered. By Convertible Bondholders' Exhibit 2 a reduction from \$328,567,293 at the end of 1939 to \$303,155,694 as of April 30th, 1946 was established. The total reduction amounted to \$25,411,598 (R. 244-248). These figures were not before the District Court at the time of the approval of the plan. These figures demonstrate the benefit of the accumulation of war-time earnings, and constitute justification for a reconsideration of the plan by the I. C. C.

Convertible Bondholders' Exhibit No. 4 shows that the sum of \$5,878,171 was spent on road and equipment during the first four months of 1946. This is in excess of the amount spent for the full two years of 1940 and 1941. It, too, shows the lasting effects of war-time earnings. It, too, is a fact new to the Court on the proceeding for confirmation. It, too, is a substantial reason for remanding the plan.

A very important piece of evidence brought to the attention of the District Court concerned the reduction of fixed charges of the Debtor. The undisputed testimony of William P. Walpole, Chief executive officer of Rock Island (R. 194; 213-214) under direct examination by the attorney for the Convertible Bondholders' group showed annual reduction of fixed charges as follows:

	Amount	Int. Rate	Fixed Charges Eliminated
R.F.C. SECURITIES			
Collateral Note ..	\$2,500,000	2½%-1½%	\$ 62,500.00
First Mtg. Bonds .	4,070,874	4%	162,834.96
Gen'l Mtg. Bonds .	5,992,850	4%	259,687.25
CHOCTAW & MEMPHIS SECURITIES			
New C. & M. Bonds	3,524,000	4%	140,960.00
Equipment obligations	21,013,208*	2½% (Av)	525,330.20

Total annual reduction of fixed charges \$1,151,312.41

The record shows that the amount of fixed interest charges was basic in the composition of the plan. The I. C. C. stated:

"It is our opinion that, in order to provide a margin for minimum additions and betterments, the fixed interest charges of the reorganized company should not exceed \$2,400,000."** (242 I. C. C. 298; TR. 142.)

Thus the annual fixed charges have been reduced by 48% of the maximum amount permitted by the I. C. C. This clearly indicates the need for a complete reconsideration and revision of the plan by the I. C. C.

The I. C. C., and not the Courts, should be charged with the duty and given the opportunity of appraising the effect of this annual saving upon the proposed capital structure of the reorganized company.

V

The District Court did not have the right to modify the plan without the prior approval of the Commission.

* The sum of \$21,013,208 represents reduction of equipment obligations of \$16,512,208 and elimination of Trustees' certificates of indebtedness in the amount of \$4,500,000 (R. 245; conv. Bondh. Ex. No. 2).

** The respondents had contended that \$3,600,000. is a conservative figure for prospective annual fixed charges (TR. 142).

Section 77 (d) of the Bankruptcy Act provides (*ante*, p. 23), in part, as follows:

"No plan shall be approved or confirmed by the judge in any proceeding under this section unless the plan shall first have been approved by the Commission and certified to the court."

Section 77 (e) defines the rights and prerogatives of the Court after certification to it of a plan by the I. C. C. and after the plan has been rejected by one or more classes of creditors. That section gives the District Court the right to confirm the plan, dismiss the proceedings or remand the plan to the I. C. C. for reconsideration and revision. Nowhere in the Act is the Court given the right to modify the plan, either upon approval or upon confirmation.

It is respectfully submitted that the plan, *as it now exists*, has not been approved by the Commission or certified by it to the Court. The last report of the Commission is dated May 1st, 1944. On November 8th, 1944, the Court ordered the claim of the R. F. C. paid. As a result thereof, collateral securities valued at over \$40,000,000 were returned to the Debtor. On June 15th, 1945, the Court ordered that the present Choctaw & Memphis Bonds shall remain undisturbed in the reorganization, in contradiction to the ruling by the I. C. C. that the Choctaw and Memphis bondholders were to receive new 4% bonds. (257 I. C. C. 265, at p. 284; TR. 259, footnote 1, to Appendix A.)

Not only must the Commission pass upon these modifications to the plan under the above quoted portion of Section 77 (d), but it should have an opportunity to appraise the effect of these changes upon the remainder of the plan.

This is particularly true in the light of a 3½% premium being paid by the Trustees for purchase of the

Choctaw bonds and the Commission's express statement that payment of the R. F. C. loan "would necessitate material modification of the plan" (TR. 234).

This Court has said, in *Ecker v. Western Pacific Railway Co.*, 318 U. S. 448, at page 474:

"Thus limited the district court acts concerning the plans only upon the issues specifically delegated by sub-section (e). As to these, its powers are negative. It may veto the plan in its entirety but may improve it only by suggestion."

The order of the Circuit Court, requiring the District Court to confirm a plan not approved by the Commission or certified by it to the Court, was reversible error.

VI

General Mortgage bondholders are *overcompensated* under the plan.

The Circuit Court of Appeals in its opinion reversing the District Court and directing confirmation of the plan found that the General Mortgage bondholders were fully compensated, taking the new \$100 par value common stock at \$50 per share.

The Court, in its opinion, said:

"The Choctaw & Memphis First Mortgage Bonds are wholly satisfied. The holders of the General Mortgage Bonds would receive new bonds and stock, satisfying their claims in full" (Add. R. 333).

But the General Mortgage bondholders are, in fact, *overcompensated*. This is easily demonstrated by the following:

1. The Commission, in its Supplemental Report of January 3, 1944, 255 I. C. C. 265, 271, so stated in these words:

"It is true that we previously found that the re-organization securities allotted to certain of the creditors accorded them full compensation for their claims. * * *

Those findings, however, were based upon the then existing situation * * *. We do not construe our previous findings to be inconsistent with the allotment of a larger amount of new mortgage bonds to the creditors from bonds which are *now* available for distribution." (Italics ours.) (TR. 233).

Considering that the proposed capitalization was also simultaneously reduced from \$368,127,410 in October 1941 (249 I. C. C. 297, pp. 302-303) to the present proposed capitalization of \$356,117,327 in January, 1944 (257 I. C. C. 265, p. 285, Appendix B, 285, 291), it is clear that the General Mortgage newly added securities are at the direct expense of junior participation.

2. The new senior securities allotted to the General Mortgage bondholders have the following *overcompensating* features:

(a) Allotment of \$1,569.36 per \$1000 of claim as follows:

\$ 189.14	in cash
143.73	in new first mortgage 4% bonds
454.14	in new income 4½% bonds
445.98	in new cumulative 5% preferred stock
336.37	in common stock

\$1,569.36 per \$1,000 of claim

(b) The maintenance of the present effective date of the plan, January 1, 1944, results in giving the General Mortgage bondholders cash and income on the above securities at a composite rate of about $4\frac{3}{4}\%$ on \$1,569.36 of securities instead of 4% interest on \$1,000 of claim. The net result is a loss to the general fund of the railroad in excess of \$500,000 per year. The General Mortgage bondholders, at the rate of interest called for by the bonds, would receive \$2,463,000 per year in interest. Interest and dividends payable to these bondholders under the plan amounts to \$2,975,000 per year, an increase of over 20%. In effect it amounts to payment of interest upon accumulated interest.

(c) The new bonds have the benefit of a sinking fund.

(d) The new bonds are convertible at the option of the holder into shares of preferred stock or common stock at the rate of \$1,000 principal amount of bonds for 10 shares of stock, and the mortgage shall contain such provisions to protect against dilution of conversion rights as the reorganization managers may determine.

(e) The new preferred stock has:

i. voting rights share for share with the common stock and may control the board of directors of the reorganized company.

ii. The new preferred stock has a 5% cumulative dividend and is convertible share for share with the new common stock and provision is made against the dilution of the conversion rights.

(f) All unpaid interest is recognized and given the equivalent treatment of unpaid principal.

(g) Common stock is also allotted in a new sharply curtailed capitalization. The Circuit Court of Appeals evaluates this \$100 par value stock at \$50 per share in

arriving at the conclusion that the General Mortgage bondholders are fully compensated.

3. Whereas, the original plan of reorganization in 1940 (242 I. C. C. 298, 438, Appendix footnote 2, TR. 142) provided that the Debtor could use new first mortgage bonds "to be sold to provide new money, or not to exceed \$11,000,000 may be borrowed and new first mortgage bonds pledged as security for the loan", upon the hearing to confirm the plan, in June 1946, however, the District Court had before it, undisputed proof of a total increase in value of Debtor's property in April, 1946 over January, 1940 to \$185,241,485.56 including \$82,272,199.08 in cash (Convertible Bondholders Exhibits Nos. 1, 2, 3 and 4; R. 244-245).

In these unanticipated and vastly improved circumstances since 1938, the total actual values of the General Mortgage new securities today are clearly in excess of their total claims.*

VII

The burden of establishing fairness of the plan, after rejection by one or more classes of creditors, is upon the proponents of the plan. That burden has not been met.

* The Commission at the time felt that "The amounts required to discharge the claims of the mortgage trustees for compensation and expenses, all costs of administration and all other allowances made or to be made by the judge in reorganization proceedings, including allowances provided for in section 77 (c) (12) of the act, should be paid in cash from the proceeds of the sale of the \$11,000,000 of new first-mortgage bonds or the loan of not to exceed \$11,000,000 secured by pledge of new first-mortgage bonds, as heretofore provided" (242 I. C. C. 298, 464). The cash position was so low! How radically the picture has changed!!

The applicable portion of Section 77 (e) of the Bankruptcy Act reads:

"That if the plan has not been so accepted by the creditors and stockholders, the judge may nevertheless confirm the plan if he is satisfied and finds, after hearing, that it makes adequate provision for fair and equitable treatment for the interests or claims of those rejecting it; that such rejection is not reasonably justified in the light of the respective rights and interests of those rejecting it and all the relevant facts; and that the plan conforms to the requirements of clauses (1) to (3), inclusive of the first paragraph of this subsection (e)."

Clauses (1) to (3), above referred to, read as follows:

"After such hearing * * * the judge shall approve the plan *if satisfied* that: (1) It complies with the provisions of subsection (b) of this section, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the law of the land regarding the participation of the various classes of creditors and stockholders; (2) the approximate amount to be paid by the debtor * * * for expenses and fees * * * etc.; (3) the plan provides for the payment of all costs of administration * * * etc." (italics ours.)

The applicable portions of the statute may be summarized to express, as a condition precedent to the confirmation of the plan, that the judge *must be satisfied and find*:

1. That the plan makes adequate provision for fair and equitable treatment of creditors rejecting the plan;
2. That the rejection of the plan by such creditors was not justified;

3. That the plan is fair and equitable;
4. That the plan affords due recognition to the rights of each class of creditors;
5. That the plan does not discriminate unfairly in favor of any class of creditors; and
6. That the plan conforms to the law of the land regarding the participation of the various classes of creditors.

"It is a fundamental rule that the burden of proof rests upon the party who, as determined by the pleadings, asserts the affirmative of the issue and it remains there until the termination of the action. It is generally on the party who will be defeated if no evidence relating to the issue is given on either side."

Reliance Life Ins. Co. v. Burgess, 112 Fed. (2nd) 234, cert. den. 304 U. S. 569.

See also:

Lilienthal v. U. S., 97 U. S. 237, 24 L. Ed. 901;
N. Y. Life Ins. Co. v. Stoner, 109 Fed. (2nd) 874;
Gilmore v. U. S., 93 Fed. (2nd) 774, cert. den. 304 U. S. 569.

There has been no attempt by the proponents of the plan to meet this burden of proof. The record at the hearing before the District Court shows that the proponents introduced no testimony, and offered into evidence only one exhibit, designated: *Estimated Income Account for Five Months Ended May 31, 1946 Compared with Actual for Same Period of 1945* (R. 239-240). The unreliability of such an estimate is borne out by the subsequent earnings.

The statute requires the above summarized findings as a condition precedent to confirmation. Such findings cannot properly be plucked out of the air. They must be supported by evidence in the record. If no such evidence exists, confirmation must be denied.

The failure of the Circuit Court to recognize these principles, to assign, pursuant to them, the burden of proof to the proponents, and to recognize that such burden of proof has not been met, all constitute reversible error.

VIII

The method of appointment of the five reorganization managers under Article XIV is not only unfair and inequitable, it is obsolete.

The original report of the Commission provided (242 I. C. C. 298, at p. 460): *

“Miscellaneous provisions—There should be five reorganization managers who should carry out the plan under the supervision and control of the court. One of such reorganization managers should be appointed by the general-mortgage committee, one by the first and refunding committee, one by the trustee under the indenture under which the debtor’s 30-year convertible bonds were issued, one by the Finance Corporation (R. F. C.) and bank creditors, and one by the committees representing the Choctaw & Memphis, Choctaw, Kansas City Short Line and Rial bonds.”

For some reason which was never satisfactorily explained by the Commission, the above provision was

* These provisions are omitted from the printed record of the I. C. C. as “obsolete”. See TR. 150.

changed on May 1, 1944 to read as follows (TR. 26):

"XIV. REORGANIZATION MANAGERS

There shall be five reorganization managers who shall carry out the plan under the supervision and control of the court. Subject to the ratification of the court, one of such reorganization managers shall be appointed by the protective committee for holders of the Chicago, Rock Island & Pacific Railway Company general-mortgage 4% bonds; one by the protective committee for holders of the Chicago, Rock Island & Pacific Railway Company first and refunding mortgage 4-percent bonds and secured 4½% bonds, series A; one jointly by the trustees for the Chicago, Rock Island & Pacific Railway Company general mortgage, its first and refunding mortgage and its secured 4½% bonds, series A; one by the Reconstruction Finance Corp'n. and bank creditors; * and one by the protective committees for holders of the Choctaw & Memphis Railroad first-mortgage 5-percent bonds * and Choctaw, Oklahoma & Gulf Railroad Company consolidated-mortgage 5-percent bonds, Burlington, Cedar Rapids & Northern Railway Company consolidated first mortgage 5-percent bonds, the St. Paul & Kansas City Short Line Railroad Company first-mortgage 4½ percent bonds, and the Rock Island, Arkansas & Louisiana Railroad Company (RIAL) first-mortgage 4½ percent bonds, and the trustee under the indenture under which the Chicago, Rock Island & Pacific Railway Company's 30 year convertible bonds were issued."

A comparative analysis by this honorable Court of the above two provisions of the I. C. C. is earnestly invited, to

* By court order of November 8, 1944, the Reconstruction Finance Corporation's claim was paid, and by court order of June 15, 1945, the court ordered that the Choctaw & Memphis Railroad Company bonds shall remain undisturbed and unaffected by the reorganization.

show the gross unfairness in: eliminating the convertible bondholders the fourth largest creditor interest in these proceedings from adequate representation among the managers, in maintaining an antiquated provision with respect to the vacancy caused by elimination of R. F. C. and bank creditors; and, in giving the general mortgage and first and refunding and secured $4\frac{1}{2}\%$ mortgage bonds control of four out of the five reorganization managers, where they only had two such managers in the original plan.

In other words, since 1940, the date of the original plan, despite the elimination of creditor classes and the improved financial earnings picture for the unsecured creditors, they are progressively and unnecessarily crowded out of the reorganization scheme so that where before they could nominate one manager, they now are given the right of a one-half vote in the designation of only one reorganization manager. Further, this right, according to the plan, is not even given to the Convertible bondholders themselves. It is given to the Chase National Bank. In view of the dual and conflicting relationship demonstrated above (Points I and II herein), the Convertible bondholders can be fairly said now to have absolutely no voice in the appointment of reorganization managers, despite the fact that they are the fourth largest class of creditors. This is strongly evidenced by the fact that the Chase Bank has joined with the other banks and indenture trustees, whose interests throughout these reorganization proceedings have been in direct conflict with those of the Convertible bondholders, in the application for the appointment of the reorganization managers.

In commenting on this situation, the District Court stated, in its opinion with respect to confirmation (see opinion, page 62, 65), rendered May 23, 1947, as follows:

"Four of the five reorganization managers, are to be appointed under the plan by committees, former members of committees or banks. The personnel of

these committees are persons who are themselves bankers or representatives of large eastern insurance companies. The power of appointment lodged in the committee for the holders of the Rock Island First and Refunding Mortgage 4% Bonds and Secured 4½% Bonds, Series A, is to be exercised by Mr. Dwight Beebe, former Chairman thereof, and Vice-President and Treasurer of the Mutual Life Insurance Company of New York. The only securities still on deposit with said committee, which is defunct, are owned by the Metropolitan Life Insurance Company. Although the power was inherited, under the Plan, by Mr. Beebe, apparently the nomination made by Mr. Beebe stemmed from Mr. Harry C. Hagerty, Treasurer of the Metropolitan Life Insurance Company, according to the report filed by Mr. E. E. Brown.

Of the twenty-nine directors of the Metropolitan Life Insurance Company, seventeen are directors or officers of banks, located principally in New York. Two of the directors of this insurance company are directors of the Bankers Trust Company of New York which, as the indenture trustee under the Rock Island General Mortgage, has a right jointly with the National City Bank of New York and Central Hanover Bank of New York, as indenture trustee of other mortgages, in the appointment of one of the other Reorganization Managers. Four of the directors of this insurance company are directors of the Chase National Bank of New York which, together with five committees, exercises a joint right in the nomination of another Reorganization Manager."

As was said in *Blumgart v. St. Louis-San Francisco R'y Co.*, 94 F. (2d) 712 (C. C. A. 8th Circ., 1938), at page 716:

"The bondholders are the creditors under a mortgage. *Bitker v. Hotel Duluth Co.* (8th Circ.), 83 F.

(2d) 721, certiorari denied 299 U. S. 577, 57 Sup. Ct. 41, 81 L. Ed. 425; (and numerous cases cited)."

In *Bitker v. Hotel Duluth Co.*, 83 F. (2d) 721, *supra*, the Court said at page 723:

"Congress, in legislating did not place a trustee in the position of censor of plans of reorganization. A trustee to so act must be a duly authorized agent for the purpose as suggested in subdivision (b) § 77B, of the act (11 U. S. C. A. § 207 b). The creditors' beneficial interests are not to be impaired by a trustee exercising such power unless it clearly appears that such power has been given * * *

The trustee's judgment must not be substituted for that of the real creditors who are to be safe-guarded in passing upon the question of whether a plan is fair and equitable."

At page 724 of the Reporter, the Court said:

"The act provides (11 U. S. C. A. Sec. 207), subsection (f) that 'before or after a plan is confirmed, changes and modifications may be proposed therein by any party in interest and may be made with the approval of the judge after hearing upon notice to creditors and stockholders'. But, as it appears, a trustee has no such interest as would entitle him to attack a plan of reorganization under this provision of the statute."

The plan must be revised to amend Article XIV thereof to permit an equitable appointment of reorganization managers by the creditors themselves, and to allow the Convertible bondholders the right to appoint at least one such manager.

IX

Respondents will undoubtedly stress the fact that this proceeding has been pending for a long time and that there must be an end to litigation. It is only fair that this honorable Court be informed as to the reasons for this delay.

These proceedings were commenced in June, 1933. For more than five (5) years following, respondents sought foreclosure of the collateral loans (See Points I and II, *supra*) to get control of the railroad without a plan of reorganization, by invalidating the reorganization statute Section 77 of the Bankruptcy Act, as amended (T. R. 32, 242 I. C. C. 299). In this dilatory activity they were unsuccessful. See *Chase Nat'l Bank, et al. v. Chicago, Rock Island & P. R'y Co.* (1935), 294 U. S. 648.

Not until July, 1938, however, did respondents prepare the plan adopted by the Interstate Commerce Commission (T. R. 32, 242 I. C. C. 299) to which the District Court has denied confirmation.

For years the respondents blocked petitioners' efforts to pay off the Reconstruction Finance Corporation loans, and even entered an appeal to the United States Circuit Court of Appeals to prevent payment of these loans, which appeals they later abandoned.

They fostered an equipment lien controversy for years, which redounded to no one's benefit. They urged compromise payment of the Choctaw & Memphis "interest on interest" claims, which claims this honorable Court properly refused to acknowledge. See *Fleming v. Traphagen*, 67 Sup. Ct. 365, 329 U. S. 686, *supra*, p. 3.

The foregoing are some of the time-consuming delays about which the respondents will say nothing.

What has been the effect of the delay?

1. The senior creditors have received an interim distribution of cash on interest in arrears and new securities amounting to \$50,000,000. The treasury of the debtor now has over \$83,000,000 in additional cash and has been earning all charges on its present capitalization since 1940, the year the plan was announced by the I. C. C.

2. The railroad is in better physical shape than ever before in its history and is earning more money since 1940, than ever before. Deferred maintenance charges are at a minimum.

3. The public interest is meanwhile being protected by the capable and successful operation and administration of the Rock Island by the reorganization court.

The question posed is whether under such circumstances the time and efforts and money expended shall be wasted, as well as the attention and energy of the Courts including the District Court, his counsel, Trustees for the Debtor and an imposing roster of counsel by the confirmation of a plan that is predicated on depression-era earnings manifestly obsolete and unfair to the holders of the convertible bonds, and was so found by the District Court after the conduct of hearings, the consideration of evidence, the reading of briefs and the study of a voluminous record.

We respectfully submit that if there has been delay in reorganizing the Rock Island, the fault has been principally that of the respondents. However, no one has been prejudiced by such delay. It cannot be the sense of Section 77(e) of the Bankruptcy Act, that creditors' property should be taken from them without due process of law, in the interest of haste. On the contrary, Section

77 has made possible the formulation of a fair and equitable plan where all creditors at least may be fully compensated, and such a plan is the true objective of this proceeding.

Conclusion

Petitioners respectfully submit that the decision of the Circuit Court of Appeals for the Seventh Circuit is erroneous; that the short-cut procedure advocated by said Court is a taking of petitioners' property without due process of law; that the questions here involved are also questions of general and public importance in the administration of the Bankruptcy Act; that it is in the public interest to have the order of said Circuit Court reversed forthwith and the plan remanded to the Interstate Commerce Commission for further proceedings; that said order of the Circuit Court should, in any event, be reviewed by this Court, to the end that the order of said Circuit Court be reversed and the decision and order of the District Court be reinstated.

Dated, July 4, 1947.

Respectfully submitted,

✓ HARRY KIRSHBAUM,
MICHAEL GESAS,
Counsel for Petitioners.

JOHN E. STONE, Esq.,
of Counsel.

(Dated May 23, 1947.)

IN THE
DISTRICT COURT OF THE UNITED STATES
FOR THE NORTHERN DISTRICT OF ILLINOIS,
EASTERN DIVISION.

In the Matter of	} No. 53209.
THE CHICAGO, ROCK ISLAND AND PACIFIC	
RAILWAY COMPANY,	
Debtor.	

OPINION WITH RESPECT TO CONFIRMATION OF
PLAN OF REORGANIZATION.

The Plan of Reorganization with which this opinion is concerned is more fully identified in the order of confirmation entered concurrently with the filing hereof. As found in the order of confirmation, the court is satisfied that it has jurisdiction over the subject matter of these proceedings and over the Debtor and the subsidiary Debtors and their properties and all creditors and stockholders thereof and all others having claims against or interests in the Debtor, the subsidiary Debtors and their properties.

Further, the court is satisfied that the Plan has been accepted by or on behalf of creditors of each class to which submission is required under subsection (e) of Section 77 holding more than two-thirds in amount of the total of the allowed claims of such class which have been reported in said submission as voting on said Plan, and that such acceptances have not been made or procured

by any means forbidden by law, and that the rejection of the Plan by creditors of classes 14 and 21-A shall be disregarded, for the purpose of confirming the Plan, pursuant to the provisions of the mandate dated April 17, 1947, of the United States Circuit Court of Appeals for the Seventh Circuit, for the reasons expressed in said mandate.

The Court is further satisfied that the Plan, under the condition to confirmation prescribed in the Order of Confirmation, conforms to the requirements of Clauses 1 to 3, inclusive, of the first paragraph of subsection (e) of Section 77 of the Bankruptcy Act and that all of the statutory requirements prerequisite to the confirmation of the Plan have been met and duly observed.

The Court is of the opinion that by virtue of said mandate, the order of this Court entered on June 28, 1946, directing that the Plan be not confirmed, has been vacated with costs, and that it is incumbent upon the Court to confirm the Plan with its present essential provisions undisturbed.

In the previous opinion of the Court, entered on June 15, 1945, correcting, clarifying and approving the plan, the view was expressed that the Reorganization Managers stand, in effect, in a fiduciary relationship towards all parties concerned in the carrying out and consummation of the Plan and should therefore be free from any special allegiance to any single class or group of creditors. It was also stated that the reorganization managers have many important functions and duties, pursuant to the provisions of the Plan, the exercise and performance of which will in a large measure determine the success and future welfare of the reorganized railroad. It is desirable to expand this view in this opinion.

The reorganization of an insolvent railroad under Section 77 involves the resolution of the conflicting interests

of the various classes of security holders as between themselves with due regard to the rights of the public at large.

The Plan is worked out as to its substantive provisions between representatives of the security holders and the Interstate Commerce Commission, a public agency, under the aegis of the Court, which determines that no legitimate interest, including the public interest, is improperly dealt with. After acceptance of the Plan by the security holders, and confirmation thereof by the Court, the function of the Court is to supervise and control the carrying out and consummation of the Plan to the end that the various classes of security holders receive the consideration for which they bargained and that the public interest is adequately protected. An important element in the exercise of this function is to guarantee that the reorganized railroad will start out with a sound and progressive management so that the public at large as well as its security holders will enjoy maximum benefits from its future operations.

The nomination of the personnel of the reorganization managers, brought home to this Court the inherent danger in the provisions of the Plan with reference to the appointment of Reorganization Managers. The nomination disclose that the majority of the reorganization managers would, if these nominations were approved, consist of officers or directors of three large Chicago banks, who were nominated by representatives of eastern banks or insurance companies, acting directly or in the name of committees, ostensibly for security holders, some of which committees are defunct or in the process of being dissolved.

The primary purpose of the provisions of the Plan with respect to the nomination of Reorganization Managers was to give to the representatives of various

creditor groups a voice in the naming of the persons who will carry out and consummate the plan. However, the Reorganization Managers must act for the benefit of all security holders and in the public interest. The Court questions whether the various creditor groups will be effectively represented by virtue of the nominations made, and believes, in any event that the public interest will not be effectively served by these nominations. The motion to ratify the nomination of Reorganization Managers was a joint motion of the committee or their former chairman and the banks, acting together, and evidences a united effort on behalf of eastern banks and insurance companies to name a banker-controlled reorganization board and ultimately a banker-controlled management for the reorganized railroad.

Four of the five reorganization managers, are to be appointed under the plan by committees, former members of committees or banks. The personnel of these committees are persons who are themselves bankers or representatives of large eastern insurance companies. The power of appointment lodged in the committee for the holders of the Rock Island and Refunding Mortgage 4% Bonds and Secured 4½% Bonds, Series A, is to be exercised by Mr. Dwight Beebe, former Chairman thereof, and Vice-President and Treasurer of the Mutual Life Insurance Company of New York. The only securities still on deposit with said committee, which is defunct, are owned by the Metropolitan Life Insurance Company. Although the power was inherited, under the Plan, by Mr. Beebe, apparently the nomination made by Mr. Beebe stemmed from Mr. Harry C. Hagerty, Treasurer of the Metropolitan Life Insurance Company, according to the report filed by Mr. E. E. Brown.

Of the twenty-nine directors of the Metropolitan Life Insurance Company, seventeen are directors or officers of banks, located principally in New York. Two of the di-

rectors of this insurance company are directors of the Bankers Trust Company of New York which, as the indenture trustee under the Rock Island General Mortgage, has a right jointly with the National City Bank of New York and Central Hanover Bank of New York, as indenture trustee of other mortgages, in the appointment of one of the other Reorganization Managers. Four of the directors of this insurance company are directors of the Chase National Bank of New York which, together with five committees, exercises a joint right in the nomination of another Reorganiaztion Manager.

In passing, it will be observed that each of five directors of the Metropolitan Life Insurance Company are directors of more than one bank.

It is also significant that, according to the report of Mr. E. E. Brown, not only that his invitation to become a Reorganization Manager came from Mr. Hagerty of the Metropolitan Life Insurance Company, but that Mr. Hagerty apparently confined his search for a candidate to the personnel of the First National Bank of Chicago, requesting first a Vice-President, then the President and ultimately the Chairman of that institution to serve.

In connection with the power of nomination exercisable by the three indenture trustees jointly, Mr. James Norris, principally a grain speculator and also director of the First National Bank of Chicago, was originally nominated. As shown by the records in this cause, Mr. Norris and his associates acquired a large amount of securities of the Debtor during the course of these bankruptcy proceedings. It appears that when Mr. Norris was confronted with the court's order to disclose his holdings and the loans made in connection therewith, he withdrew his name as a nominee, and the banks which nominated him substituted in his place Mr. Charles D. Wiman, a director of the Continental Illinois National Bank and Trust Company of Chicago.

It is further appropriate to observe that the three banks which as indenture trustees nominated Mr. Wiman, are fiduciaries for the mortgage issues, the so-called protective committees for which nominated Mr. Roy Ingersoll and Mr. E. E. Brown. This is illustrative of the accumulative appointment powers given to the same underlying interests.

In connection with Mr. Wiman, his report does not conform to the order of the Court requiring full disclosure of the circumstances surrounding his nomination in that he did not see fit to state who, on behalf of the three banks which nominated him, asked him to serve as a Reorganization Manager.

The reticular affiliations of the Banker-Insurance group and their nominees is illustrative anew in connection with the nomination of Mr. Roy Ingersoll by the General Mortgage Committee. This gentleman is a member of the Board of Directors of the Transportation Association of America, the Chairman of which is a vice-president of the Metropolitan Life Insurance Company. Also, Mr. Edward E. Brown, Chairman of the First National Bank of Chicago, is a Trustee of the Penn Mutual Life Insurance Company, the general counsel for which is a member of the General Mortgage Bondholders Committee which nominated Mr. Ingersoll.

The provisions of the Plan giving the Reconstruction Finance Corporation, the Continental Illinois Bank and the other bank creditors, a joint right to nominate one of the reorganization managers no longer has any degree of validity in these proceedings, as those institutions have long since been repaid their loans. No attempt was made to exercise this particular right of nomination, apparently leaving this right to be exercised by the Court.

Finally, it may be observed that with respect to the nominative power lodged jointly in five committees of the

subsidiary debtors bondholders and the First National Bank of New York, as indenture trustee for one of the mortgage issues, one committee is defunct, another is being dissolved and the third is not affected by the Plan. These committees are likewise composed of representatives of eastern banks and insurance companies.

While it is desirable to have the point of view of bankers represented on the board of Reorganization Managers, it is certainly not in the public interest to have this point of view dominate and control said board. Obviously the Court can have no confidence that any other nominees from these same sources which are composed of bankers and representatives of insurance companies would be in any way less responsive to the influence of eastern banks and insurance companies.

The Court thus is compelled to conclude that the provisions of the Plan prescribing the mechanics by means of which the plan is to be consummated are defective in lodging the power of nomination of a majority of the Reorganization Managers in bankers and representatives of insurance companies. In order to avoid this unwholesome result, the Court has determined to attach conditions to the confirmation of the Plan appropriate to the framework of the Plan and affecting only the mechanics by means of which the Plan is to be consummated which will insure that a majority of the Reorganization Managers will be responsive to the public interest.

The Circuit Court of Appeals for the Seventh Circuit has upheld the power of this Court to make summary modifications in the mechanics by which a Plan is to be consummated without changing the essence of the Plan itself.

In the case of *In re Chicago, Milwaukee & St. Paul Railroad Co.*, (C. C. A. 7) 145 F. (2d) 299, that Court, in referring to charges made in the method of selecting voting

trustees to serve as interim managers, said, on page 304:

"Furthermore, we are doubtful if this requirement is in fact a part of the Plan of Reorganization. . . . It can be more aptly described, so we think, as part of the mechanics by which the Plan is to be consummated. We are of the view that this change by the Court did not alter the Plan so as to require a re-reference to the Commission."

Similarly, in a proceeding under Sec. 77B, the Court of Appeals for this Circuit upheld the District Court's right to attach conditions to an order of confirmation of a Plan, insuring reasonable supervision over the reorganized company's early life.

In the case of *In re H. W. Clark Co.*, (C. C. A. 7) 79 F. (2d) 681, the Court said, on page 684:

"It is obvious that the Court made no modifications of the Plan. They were conditions to be complied with for the purpose of assuring the proper execution of the Plan, all of which rebounded to the benefit of the bondholders and all other creditors."

Under all of the circumstances, it appears that the public interest will best be served by a majority of the Reorganization Managers being appointed by the Court which is itself a public agency, and which will act in the public interest to insure the selection of a majority of the Reorganization Managers board responsive to the public interest.

In order to accomplish this purpose, the Court has determined to attach conditions to the confirmation of the Plan under which the court will exercise the right of appointment of three of the Reorganization Managers lodged respectively, in the three indenture trustees, jointly, and in five

committees for holders of securities of subsidiary Debtors and the First National Bank of New York, as indenture trustee for one of the mortgage issues and the Reconstruction Finance Corporation leaving undisturbed the right of appointment in others, as provided by the Plan.

The conditions to the confirmation of the Plan are set forth in the Order of Confirmation entered concurrently with the filing hereof.

Dated, May 23, 1947.

IN THE

District Court of the United States

FOR THE NORTHERN DISTRICT OF ILLINOIS,

EASTERN DIVISION.

In the Matter of

THE CHICAGO, ROCK ISLAND AND
PACIFIC RAILWAY COMPANY,
Debtor.

} No. 53209.

ORDER CONFIRMING PLAN OF REORGANIZATION.

This cause coming on to be heard upon the motion of various parties for the entry of an order herein confirming the Plan of Reorganization of the Debtor and the subsidiary Debtors, pursuant to the mandate dated April 17, 1947 of the United States Circuit Court of Appeals for the Seventh Circuit; and it appearing that no further notice is required to be given to the parties in interest herein in order to enter this order in compliance with said mandate, but that notice of said motion and of this hearing has been served by movants upon counsel for the Trustees of the properties of the Debtor and the subsidiary Debtors; and the Court having heard argument of counsel and being fully advised in the premises,

FINDS:

A. This Court has jurisdiction over the subject matter of these proceedings and over the Debtor and the subsidiary Debtors and their properties, and all creditors and stockholders thereof, and all others having claims

against or interest in the Debtor, the subsidiary Debtors, and their properties.

B. The Plan of Reorganization which is being confirmed herein pursuant to said mandate (hereinafter referred to as the "Plan of Reorganization" or the "Plan") is the plan of reorganization for The Chicago, Rock Island and Pacific Railway Company, Debtor, (hereinafter referred to as the "Debtor"), and for the St. Paul & Kansas City Short Line Railroad Company, Rock Island, Arkansas & Louisiana Railroad Company, The Chicago, Rock Island & Gulf Railway Company, Choctaw, Oklahoma & Gulf Railroad Company, Rock Island, Stuttgart and Southern Railway Company, Rock Island, Omaha Terminal Railway Company, Rock Island Memphis Terminal Railway Company and Peoria Terminal Company, subsidiary Debtors (hereinafter referred to as the "subsidiary Debtors"), which, as modified and amended, was approved by the Interstate Commerce Commission (hereinafter referred to as the "Commission") by its supplemental report and order, dated May 1, 1944, in Finance Docket No. 10028, and by said Commission certified to this Court, and which, pursuant to the opinion of this Court and filed on May 14, 1945, was corrected, clarified and approved by order of this Court entered on June 15, 1945.

C. Certified copies of the opinion of this Court filed on May 14, 1945, and of the order entered on June 15, 1945, were duly sent by the Clerk of this Court to said Commission.

D. The Trustees of the properties of the Debtor and the subsidiary Debtors filed with this Court lists (revised and supplemented from time to time) of all known bondholders and creditors of and claimants against the Debtor and the subsidiary Debtors and their respective

properties, showing the amounts and character of their debts, claims and securities, and their respective last known post office addresses of places of business, which lists, revisions and supplements were transmitted by the Clerk of this Court to said Commissions.

E. Pursuant to order of the Interstate Commerce Commission, entered on November 8, 1945, and in accordance with law, the Plan of Reorganization was submitted for acceptance or rejection to all holders of securities or claims, as of November 23, 1945, of Classes 4, 5, 13, 14, 15, 17, 18, 19, 20, 21-A and 26, said Classes being among those created by and described in the orders of this Court entered herein on January 23, 1934 and June 26, 1944. By its said order, the Commission provided that such submission be effected by mailing to each such creditor shown on the lists filed by the Trustees, and to each such creditor not so listed whose claim was allowed, and who might request a ballot, a copy of the Plan of Reorganization, together with other material specified in said order of the Commission, including a ballot, in duplicate, and a statement by the Secretary of the Commission advising such creditors of the approval and submission of the Plan, describing the method of voting and stating the limit of time within which the executed ballots must be returned to the office of the Commission, which limit of time was on or before January 7, 1946 for ballots mailed in the continental United States and January 22, 1946 for ballots executed by persons residing outside the continental United States.

F. Due notice of such submission, as aforesaid, was published by the Trustees of the properties of the Debtor and the subsidiary Debtors herein as required by the Commission and by this Court pursuant to order entered herein on November 20, 1945.

G. The Commission, by its certificate dated February 26, 1946, and filed herein on February 28, 1946, has certified to this Court, in accordance with law, the results of the submission of the Plan of Reorganization to creditors of Classes 4, 5, 13, 14, 15, 17, 18, 19, 20, 21-A and 26, as aforesaid.

H. Said submission to creditors was made by the Interstate Commerce Commission and the results thereof were certified by said Commission to this Court in all respects in the manner required by law.

I. The rejection of the Plan of Reorganization by creditors of Classes 14 and 21-A shall be disregarded, for the purpose of confirming the Plan, pursuant to the provisions of said mandate, for the reasons expressed therein.

J. Under the provisions of said mandate, the order of this Court, entered on June 28, 1946, directing that the Plan of Reorganization be not confirmed, has been vacated with costs.

K. A defect exists in the provisions of the Plan of Reorganization prescribing the mechanics by means of which the Plan is to be carried out and consummated, for the reasons stated in the opinion of the Court filed concurrently herewith. The Court has power to correct such defect in order to carry out the Plan effectively, under the law and pursuant to the provisions of the Plan. The condition to confirmation of the Plan set forth in this order is reasonable and equitable, and will serve the best interests of the Debtor, the subsidiary Debtors, their respective creditors and the public, and is not inconsistent with the provisions of the opinion and decree of the United States Circuit Court of Appeals for the Seventh Circuit, pursuant to which said mandate issued.

L. The Plan of Reorganization, under the condition to confirmation prescribed herein, conforms to the requirements of clauses (1) to (3), inclusive, of the first paragraph of subsection (e) of Section 77 of the Bankruptcy Act.

NOW THEREFORE, it is hereby ORDERED, ADJUDGED and DECREED:

That the Plan of Reorganization be and hereby is confirmed, subject to the condition that, for the reasons expressed in the opinion of this court filed concurrently herewith,

(a) In lieu of the appointment, subject to the ratification of the Court, of one of the reorganization managers, and any successor thereto, from time to time, jointly by the Trustees for the Chicago, Rock Island and Pacific Railway Company general mortgage, its first and refunding mortgage, and its secured $4\frac{1}{2}$ per cent bonds, series A; and

(b) In lieu of the appointment, subject to the ratification of the Court, of one of the reorganization managers, and any successor thereto, from time to time, by the Reconstruction Finance Corporation and bank creditors; and

(c) In lieu of the appointment, subject to the ratification of the Court, of one of the reorganization managers, and any successor thereto, from time to time, jointly by the protective committee for holders of the Choctaw & Memphis Railroad Company first-mortgage 5 percent bonds and Choctaw, Oklahoma & Gulf Railroad Company consolidated mortgage 5-percent bonds, Burlington, Cedar Rapids & Northern Railway Company consolidated first mortgage 5-percent bonds, the St. Paul & Kansas City Short Line Railroad Company first mortgage $4\frac{1}{2}\%$ percent

bonds, and the Rock Island, Arkansas & Louisiana Railroad Company First mortgage 4½ percent bonds, and the Trustee under the indenture under which the Chicago, Rock Island & Pacific Railway Company's 30 year convertible bonds were issued, or by the individuals who were formerly the chairman, or members, as the case may be, of any of said committees which are not now, or hereafter may not be, in existence;

the court shall appoint three of the reorganization managers and their respective successors from time to time.

The nominations of Reorganization Managers filed by the committees for the General Mortgage Bonds, and the First and Refunding secured 4½ percent bonds, Series A, will stand to be acted upon by the Court unless withdrawn by May 27, 1947 and the Court will act with respect to all Reorganization Managers appointments or approvals by May 28, 1947.

The Court hereby reserves jurisdiction of these proceedings and of all parties in interest herein for the purpose of entering such further and other orders as may be necessary or proper for the purpose of carrying out the Plan of Reorganization.

Costs will be allowed in accordance with the mandate of the Circuit Court of Appeals.

ENTER:

Dated

IN THE
UNITED STATES CIRCUIT COURT OF APPEALS,
FOR THE SEVENTH CIRCUIT.

No. 9387.

OCTOBER TERM, 1946, APRIL SESSION, 1947.

IN THE MATTER
of
THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY COMPANY,
Debtor.

Re Application of
J. HAMILTON CHESTON, et al.,
vs.
Petitioners,

HON. MICHAEL L. IGOE,
Respondent.

June 9, 1947.

Before MAJOR, KERNER, and MINTON, *Circuit Judges*.

Per Curiam. This is a petition for a writ of mandamus directing respondent to correct the entry of an order so as to comply with the mandate of this court as sent down *In the Matter of The Chicago Rock Island & Pacific Railway Company, Debtor, Cheston, et al. v. Chase National Bank, et al.*, 160 F. 2d . . . , in which case it was decreed that the order of the District Court refusing to confirm the plan of reorganization of the debtor be vacated and the cause be remanded to the District Court with instructions that it enter forthwith an order confirming the plan.

The plan provides for five reorganization managers to carry out the plan, each of the five to be appointed by a creditor interest or group of creditor interests, subject to the ratification of the court. The mandate of this court was duly issued and filed in the District Court and petitioners, representing various groups of secured creditors of the debtor, on May 6, 1947, moved respondent as United States District Court for an order confirming the plan of reorganization pursuant to the mandate, and for an order ratifying the designations by various creditor representatives of four reorganization managers. Reconstruction Finance Corporation and the bank creditors no longer being creditors of the debtor, no appointment was made on their behalf, but it was left to the court as provided by the plan. Respondent continued the motions to May 23 and entered an order directing all committees to file statements of all securities on deposit and that the persons designated as reorganization managers file additional information with the court. These were filed.

On May 23 respondent filed an opinion and entered an order confirming the plan, subject, however, to the condition that the court should appoint three of the reorganization managers. In other words, he took the power to appoint the managers provided in the plan to be appointed by (1) the three trustees for the debtor's General Mortgage 4% Bonds, First and Refunding Mortgage 4% Bonds, and Secured 4½% Bonds, Series A, and (2) the Divisional Creditor Group, and retained the power to appoint one manager in place of (3) Reconstruction Finance Corporation and bank creditors.

Petitioners contend that in attaching the condition that the District Court shall appoint three of the managers, respondent changed and altered the plan, and violated his ministerial duty to conform to the mandate of this court.

Before discussing petitioners' contention, it is well that we dispose of respondent's claim that even if the order

is erroneous, it "is reviewable only by appeal." With this view we cannot agree, since the courts have uniformly held that where a lower court has failed to comply with the mandate of the reviewing court, compliance with the mandate may be compelled by a writ of mandamus. See *In re Sanford Fork & Tool Co.*, 160 U. S. 247; *In re Potts*, 166 U. S. 263; *Baltimore & Ohio R. R. v. United States*, 279 U. S. 781; *United States v. United States District Court*, 272 F. 611; *United States v. Howe*, 280 F. 815.

A reading of the opinion filed by respondent at the time he entered the order on the mandate discloses that he was of the opinion that an "inherent danger" lay in the provisions of the plan with reference to the appointment of the reorganization managers, in that the plan lodged the power of nomination of a majority of the reorganization managers in bankers and representatives of insurance companies, and in order to avoid this "unwholesome result," the respondent in his opinion said he "has determined to attach conditions to the confirmation of the Plan appropriate to the framework of the Plan * * * which will insure that a majority of the Reorganization Managers will be responsive to the public interest."

The article relating to the managers was in the plan as certified to the District Court by the Interstate Commerce Commission in its report of May 1, 1944, approved by the court in June, 1945. It was in the plan as submitted by the Commission to debtor's creditors for their acceptance or rejection and thus became an integral part of the plan. It was in the plan when we affirmed the order of the District Court approving the plan, and it was in the plan when this court directed the District Court to confirm the plan forthwith. The plan, as we have already noted, definitely fixed the manner of designating the reorganization managers, and provided for their duties, rights and responsibilities. In such a situation the court had no right to substitute a means of execution of its own, con-

trary to and in derogation of the provisions of the plan.
In re Alton R. R., 159 F. 2d 200, 206.

The writ of mandamus will issue. Respondent is commanded to expunge and vacate the order of May 23, 1947, so far as it alters and changes the plan of reorganization, by striking from the order the phrase "subject to the condition that" and all of the subsequent provisions of the order down to and including the words "appointments or approvals by May 28, 1947." It is so ordered.

A true Copy:

Teste:

.....
 Clerk of the United States Circuit Court
 of Appeals for the Seventh Circuit.